

WESTERN DIGITAL CORP

FORM 10-Q (Quarterly Report)

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Sector	Technology
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**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 30, 2016

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: 1-8703

Western Digital®
WESTERN DIGITAL CORPORATION
(Exact Name of Registrant as Specified in Its Charter)

Delaware

*(State or other jurisdiction of
incorporation or organization)*

**5601 Great Oaks Parkway
San Jose, California**

(Address of principal executive offices)

33-0956711

*(I.R.S. Employer
Identification No.)*

95119

(Zip Code)

Registrant's telephone number, including area code: (408) 717-6000

3355 Michelson Drive, Suite 100, Irvine, California 92612

(Former name, former address and former fiscal year, if changed since last report)

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

Indicate by check mark whether the registrant 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 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. (Check one):

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

As of the close of business on February 3, 2017, 288,070,433 shares of common stock, par value \$0.01 per share, were outstanding.

WESTERN DIGITAL CORPORATION
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Unless otherwise indicated, references herein to specific years and quarters are to our fiscal years and fiscal quarters, and references to financial information are on a consolidated basis. As used herein, the terms “we,” “us,” “our,” the “Company,” “WDC” and “Western Digital” refer to Western Digital Corporation and its subsidiaries, unless we state, or the context indicates, otherwise.

WDC, a Delaware corporation, is the parent company of our data storage business. Our principal executive offices are located at 5601 Great Oaks Parkway, San Jose, California 95119 . Our telephone number is (408) 717-6000 , and our website is www.westerndigital.com. The information on our website is not incorporated in this Quarterly Report on Form 10-Q.

Western Digital, WD, the WD logo and SanDisk are registered trademarks or trademarks of Western Digital or its affiliates in the U.S. and/or other countries. All other trademarks, registered trademarks and/or service marks, indicated or otherwise, are the property of their respective owners.

Forward-Looking Statements

This document contains forward-looking statements within the meaning of the federal securities laws. Any statements that do not relate to historical or current facts or matters are forward-looking statements. You can identify some of the forward-looking statements by the use of forward-looking words, such as “may,” “will,” “could,” “would,” “project,” “believe,” “anticipate,” “expect,” “estimate,” “continue,” “potential,” “plan,” “forecast,” and the like, or the use of future tense. Statements concerning current conditions may also be forward-looking if they imply a continuation of current conditions. Examples of forward-looking statements include, but are not limited to, statements concerning:

- expectations concerning the anticipated benefits of our acquisition of SanDisk Corporation;*
- expectations regarding the integration of our HGST and WD subsidiaries following the decision by the Ministry of Commerce of the People’s Republic of China in October 2015;*
- expectations regarding our business strategy, our ability to execute that strategy and its intended benefits;*
- our plans to develop and invest in new products and expand into new storage markets and into emerging economic markets;*
- our quarterly cash dividend policy;*
- expectations regarding the outcome of legal proceedings in which we are involved;*
- expectations regarding the repatriation of funds from our foreign operations;*
- our beliefs regarding tax benefits and the timing of future payments, if any, relating to the unrecognized tax benefits, and the adequacy of our tax provisions;*
- expectations regarding capital investments and sources of funding for those investments; and*
- our beliefs regarding the sufficiency of our available liquidity to meet our working capital, debt, dividend and capital expenditure needs.*

Forward-looking statements are subject to risks and uncertainties that could cause actual results to differ materially from those expressed in the forward-looking statements. You are urged to carefully review the disclosures we make concerning risks and other factors that may affect our business and operating results, including those made in Part II, Item 1A of this Quarterly Report on Form 10-Q, and any of those made in our other reports filed with the Securities and Exchange Commission. You are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date of this document. We do not intend, and undertake no obligation, to publish revised forward-looking statements to reflect events or circumstances after the date of this document or to reflect the occurrence of unanticipated events.

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements (unaudited)

WESTERN DIGITAL CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS
(in millions, except par value)
(Unaudited)

	December 30, 2016	July 1, 2016
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 4,940	\$ 8,151
Short-term investments	161	227
Accounts receivable, net	2,004	1,461
Inventories	2,085	2,129
Other current assets	416	616
Total current assets	9,606	12,584
Property, plant and equipment, net	3,238	3,503
Notes receivable and investments in Flash Ventures	1,082	1,171
Goodwill	10,005	9,951
Other intangible assets, net	4,469	5,034
Other non-current assets	575	619
Total assets	\$ 28,975	\$ 32,862
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 2,012	\$ 1,888
Accounts payable to related parties	175	168
Accrued expenses	1,001	995
Accrued compensation	581	392
Accrued warranty	190	172
Bridge loan	—	2,995
Current portion of long-term debt	129	339
Total current liabilities	4,088	6,949
Long-term debt	12,944	13,660
Other liabilities	1,211	1,108
Total liabilities	18,243	21,717
Commitments and contingencies (Notes 6, 8, 10 and 14)		
Shareholders' equity:		
Preferred stock, \$0.01 par value; authorized — 5 shares; issued and outstanding — none	—	—
Common stock, \$0.01 par value; authorized — 450 shares; issued — 312 shares; outstanding — 288 shares and 284 shares, respectively	3	3
Additional paid-in capital	4,574	4,429
Accumulated other comprehensive income (loss)	(197)	103
Retained earnings	8,411	8,848
Treasury stock — common shares at cost; 24 shares and 28 shares, respectively	(2,059)	(2,238)
Total shareholders' equity	10,732	11,145
Total liabilities and shareholders' equity	\$ 28,975	\$ 32,862

The accompanying notes are an integral part of these condensed consolidated financial statements.

WESTERN DIGITAL CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(in millions, except per share amounts)
(Unaudited)

	Three Months Ended		Six Months Ended	
	December 30, 2016	January 1, 2016	December 30, 2016	January 1, 2016
Revenue, net	\$ 4,888	\$ 3,317	\$ 9,602	\$ 6,677
Cost of revenue	3,355	2,411	6,734	4,816
Gross profit	1,533	906	2,868	1,861
Operating expenses:				
Research and development	585	389	1,224	774
Selling, general and administrative	358	239	754	431
Employee termination, asset impairment and other charges	45	27	113	83
Total operating expenses	988	655	2,091	1,288
Operating income	545	251	777	573
Interest and other income (expense):				
Interest income	5	5	10	9
Interest expense	(205)	(13)	(441)	(26)
Other income (expense), net	(24)	1	(296)	2
Total interest and other expense, net	(224)	(7)	(727)	(15)
Income before taxes	321	244	50	558
Income tax expense (benefit)	86	(7)	181	24
Net income (loss)	\$ 235	\$ 251	\$ (131)	\$ 534
Income (loss) per common share				
Basic	\$ 0.82	\$ 1.08	\$ (0.46)	\$ 2.31
Diluted	\$ 0.80	\$ 1.07	\$ (0.46)	\$ 2.28
Weighted average shares outstanding:				
Basic	286	232	285	231
Diluted	294	234	285	234
Cash dividends declared per share	\$ 0.50	\$ 0.50	\$ 1.00	\$ 1.00

The accompanying notes are an integral part of these condensed consolidated financial statements.

WESTERN DIGITAL CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
(in millions)
(Unaudited)

	Three Months Ended		Six Months Ended	
	December 30, 2016	January 1, 2016	December 30, 2016	January 1, 2016
Net income (loss)	\$ 235	\$ 251	\$ (131)	\$ 534
Other comprehensive income (loss), before tax:				
Actuarial pension gain	1	—	6	—
Foreign currency translation adjustment	(186)	—	(169)	—
Net unrealized gain (loss) on foreign exchange contracts	(136)	38	(140)	13
Net unrealized loss on available-for-sale securities	—	(2)	—	(1)
Total other comprehensive income (loss), before tax	(321)	36	(303)	12
Income tax benefit related to items of other comprehensive income (loss), before tax	9	—	3	—
Other comprehensive income (loss), net of tax	(312)	36	(300)	12
Total comprehensive income (loss)	\$ (77)	\$ 287	\$ (431)	\$ 546

The accompanying notes are an integral part of these condensed consolidated financial statements.

WESTERN DIGITAL CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(in millions)
(Unaudited)

	Six Months Ended	
	December 30, 2016	January 1, 2016
Cash flows from operating activities		
Net income (loss)	\$ (131)	\$ 534
Adjustments to reconcile net income (loss) to net cash provided by operations:		
Depreciation and amortization	1,022	488
Stock-based compensation	201	79
Deferred income taxes	117	15
Loss on disposal of assets	10	6
Write-off of issuance costs and amortization of debt discounts	258	2
Loss on settlement of convertible debt	5	—
Non-cash portion of employee termination, asset impairment and other charges	13	18
Other non-cash operating activities, net	42	—
Changes in:		
Accounts receivable, net	(540)	(118)
Inventories	52	127
Accounts payable	180	(58)
Accounts payable to related parties	6	—
Accrued expenses	59	35
Accrued compensation	194	(15)
Other assets and liabilities, net	12	30
Net cash provided by operations	1,500	1,143
Cash flows from investing activities		
Purchases of property, plant and equipment	(330)	(300)
Proceeds from the sale of equipment	1	—
Purchases of investments	(239)	(408)
Proceeds from sale of investments	55	266
Proceeds from maturities of investments	279	—
Investments in Flash Ventures	(20)	—
Notes receivable issuances to Flash Ventures	(309)	—
Notes receivable proceeds from Flash Ventures	259	—
Strategic investments and other, net	(12)	(12)
Net cash used in investing activities	(316)	(454)
Cash flows from financing activities		
Issuance of stock under employee stock plans	90	54
Taxes paid on vested stock awards under employee stock plans	(40)	(44)
Excess tax benefits from employee stock plans	56	(6)
Proceeds from acquired call option	61	—
Repurchases of common stock	—	(60)
Dividends paid to shareholders	(284)	(231)
Repayment of debt	(8,254)	(63)
Proceeds from debt	3,992	—
Debt issuance costs	(7)	—
Net cash used in financing activities	(4,386)	(350)
Effect of exchange rate changes on cash	(9)	—
Net increase (decrease) in cash and cash equivalents	(3,211)	339
Cash and cash equivalents, beginning of year	8,151	5,024
Cash and cash equivalents, end of period	\$ 4,940	\$ 5,363
Supplemental disclosure of cash flow information:		

Cash paid for income taxes	\$	43	\$	21
Cash paid for interest	\$	299	\$	22
Supplemental disclosure of non-cash investing and financing activities:				
Accrual of cash dividend declared	\$	144	\$	116

The accompanying notes are an integral part of these condensed consolidated financial statements.

WESTERN DIGITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

Note 1 . Basis of Presentation

Western Digital Corporation (the “Company” or “Western Digital”) is a leading developer, manufacturer and provider of data storage devices and solutions that address the needs of the information technology industry and the infrastructure that enables the storage of data. The Company also generates license and royalty revenue related to its intellectual property.

The accounting policies followed by the Company are set forth in Part II, Item 8, Note 1 of the Notes to Consolidated Financial Statements included in the Company’s Annual Report on Form 10-K for the fiscal year ended July 1, 2016 . In the opinion of management, all adjustments necessary to fairly state the unaudited condensed consolidated financial statements have been made. All such adjustments are of a normal, recurring nature. Certain information and footnote disclosures normally included in the consolidated financial statements prepared in accordance with accounting principles generally accepted in the United States (“U.S. GAAP”) have been condensed or omitted pursuant to the rules and regulations of the Securities and Exchange Commission (“SEC”). These unaudited condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and the notes thereto included in the Company’s Annual Report on Form 10-K for the fiscal year ended July 1, 2016 . The results of operations for interim periods are not necessarily indicative of results to be expected for the full year.

Fiscal Year

The Company’s fiscal year ends on the Friday nearest to June 30 and typically consists of 52 weeks. Fiscal year 2017 , which ends on June 30, 2017 , and fiscal year 2016 , which ended on July 1, 2016 , are both comprised of 52 weeks, with all quarters presented consisting of 13 weeks.

Reclassifications

Certain prior year amounts have been reclassified in the condensed consolidated statements of operations and condensed consolidated statements of cash flows to conform to the current year presentation.

Use of Estimates

Company management has made estimates and assumptions relating to the reporting of certain assets and liabilities in conformity with U.S. GAAP. These estimates and assumptions have been applied using methodologies that are consistent throughout the periods presented. However, actual results could differ materially from these estimates.

WESTERN DIGITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
(Unaudited)

Note 2 . Accounting Changes and Recent Accounting Pronouncements

Recently Adopted

In April 2015, the Financial Accounting Standard Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2015-05, “Intangibles — Goodwill and Other — Internal-Use Software (Subtopic 350-40)” (“ASU 2015-05”), which provides guidance to customers about whether a cloud computing arrangement includes a software license. If a cloud computing arrangement includes a software license, the customer should account for the software license element of the arrangement consistent with the acquisition of other software licenses. If a cloud computing arrangement does not include a software license, the customer should account for the arrangement as a service contract. The Company’s adoption of ASU 2015-05 at the beginning of the current year did not have a material impact on its condensed consolidated financial statements.

WESTERN DIGITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
(Unaudited)

Note 3 . Supplemental Financial Statement Data*Accounts receivables*

From time to time, in connection with factoring agreements, the Company sells trade accounts receivable without recourse to third party purchasers in exchange for cash. During the three and six months ended December 30, 2016 and the three months ended January 1, 2016, the Company did not sell any trade accounts receivables. During the six months ended January 1, 2016, the Company sold trade accounts receivable and received cash proceeds of \$200 million. The discounts on the trade accounts receivables sold during the six months ended January 1, 2016 were not material and were recorded within Other income (expense), net in the condensed consolidated statements of operations.

Inventories

	December 30, 2016	July 1, 2016
<i>(in millions)</i>		
Inventories:		
Raw materials and component parts	\$ 586	\$ 569
Work-in-process	617	589
Finished goods	882	971
Total inventories	<u>\$ 2,085</u>	<u>\$ 2,129</u>

Property, Plant and Equipment

	December 30, 2016	July 1, 2016
<i>(in millions)</i>		
Property, plant and equipment:		
Land and buildings	\$ 1,871	\$ 1,900
Machinery and equipment	7,064	6,915
Software	174	155
Furniture and fixtures	52	110
Leasehold improvements	314	307
Construction-in-process	119	245
Property, plant and equipment, gross	9,594	9,632
Accumulated depreciation	(6,356)	(6,129)
Property, plant and equipment, net	<u>\$ 3,238</u>	<u>\$ 3,503</u>

Goodwill

	Carrying Amount
<i>(in millions)</i>	
Balance at July 1, 2016	\$ 9,951
Purchase price adjustments to goodwill	60
Foreign currency translation adjustment	(6)
Balance at December 30, 2016	<u>\$ 10,005</u>

The purchase price adjustments resulted from adjustments to the assessment of fair value for certain acquired intangible assets; inventory; property, plant and equipment; and a portion of the deferred tax liability related to the acquisition of SanDisk Corporation ("SanDisk").

WESTERN DIGITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
(Unaudited)

Intangible Assets

	December 30, 2016	July 1, 2016
	<i>(in millions)</i>	
Finite-lived intangible assets	\$ 5,203	\$ 3,539
In-process research and development	695	2,435
Accumulated amortization	(1,429)	(940)
Intangible assets, net	<u>\$ 4,469</u>	<u>\$ 5,034</u>

Acquired in-process research and development (“IPR&D”) is accounted for as an indefinite-lived intangible asset. Upon completion of development, IPR&D is considered to be an amortizable finite-lived intangible asset. During the three months ended December 30, 2016, the Company reclassified \$1.7 billion of acquired IPR&D to existing technology and commenced amortization over an estimated useful life of 4 years.

Product Warranty Liability

Changes in the warranty accrual were as follows:

	Three Months Ended		Six Months Ended	
	December 30, 2016	January 1, 2016	December 30, 2016	January 1, 2016
	<i>(in millions)</i>			
Warranty accrual, beginning of period	\$ 277	\$ 218	\$ 279	\$ 221
Charges to operations	44	43	91	88
Utilization	(35)	(40)	(80)	(94)
Changes in estimate related to pre-existing warranties	27	4	23	10
Warranty accrual, end of period	<u>\$ 313</u>	<u>\$ 225</u>	<u>\$ 313</u>	<u>\$ 225</u>

The long-term portion of the warranty accrual classified in other liabilities was \$123 million and \$107 million as of December 30, 2016 and July 1, 2016, respectively.

Accumulated Other Comprehensive Income (Loss)

Other comprehensive income (loss) (“OCI”), net of tax refers to expenses, gains and losses that are recorded as an element of shareholders’ equity but are excluded from net income. The following table illustrates the changes in the balances of each component of accumulated other comprehensive income (loss) (“AOCI”):

	Actuarial Pension Gains (Losses)	Foreign Currency Translation Gains (Losses)	Unrealized Gains (Losses) on Foreign Exchange Contracts	Total AOCI
	<i>(in millions)</i>			
Balance at July 1, 2016	\$ (45)	\$ 74	\$ 74	\$ 103
OCI before reclassifications	6	(169)	(98)	(261)
Amounts reclassified from AOCI	—	—	(42)	(42)
Income tax benefit (expense) related to items of OCI	(2)	5	—	3
Net current-period OCI	4	(164)	(140)	(300)
Balance at December 30, 2016	<u>\$ (41)</u>	<u>\$ (90)</u>	<u>\$ (66)</u>	<u>\$ (197)</u>

WESTERN DIGITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
(Unaudited)

The following table illustrates the significant amounts of each component reclassified out of AOCI to the condensed consolidated statements of operations:

AOCI Component	Three Months Ended		Six Months Ended		Statement of Operations Line Item
	December 30, 2016	January 1, 2016	December 30, 2016	January 1, 2016	
<i>(in millions)</i>					
Unrealized holding gain (loss) on cash flow hedging activities:					
Foreign exchange contracts	\$ 16	\$ (25)	\$ 40	\$ (53)	Cost of revenue
Foreign exchange contracts	—	—	2	—	Research and development
Unrealized holding gain (loss) on cash flow hedging activities	16	(25)	42	(53)	
Total reclassifications for the period	\$ 16	\$ (25)	\$ 42	\$ (53)	

WESTERN DIGITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
(Unaudited)

Note 4. Fair Value Measurements and Investments*Financial Instruments Carried at Fair Value*

Financial assets and liabilities that are remeasured and reported at fair value at each reporting period are classified and disclosed in one of the following three levels:

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

Level 2. Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; 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 unobservable for the asset or liability and that are significant to the fair value of the assets or liabilities.

The following tables present information about the Company's financial assets and liabilities that are measured at fair value on a recurring basis as of December 30, 2016 and July 1, 2016, and indicate the fair value hierarchy of the valuation techniques utilized to determine such values:

	December 30, 2016			
	Level 1	Level 2	Level 3	Total
	<i>(in millions)</i>			
Assets:				
Cash equivalents:				
Money market funds	\$ 1,381	\$ —	\$ —	\$ 1,381
Certificates of deposit	—	8	—	8
Total cash equivalents	1,381	8	—	1,389
Short-term investments:				
Certificates of deposit	—	137	—	137
Corporate notes and bonds	—	13	—	13
Asset-backed securities	—	7	—	7
Municipal notes and bonds	—	4	—	4
Total short-term investments	—	161	—	161
Long-term investments:				
U.S. Treasury securities	2	—	—	2
U.S. Government agency securities	—	5	—	5
International government securities	—	1	—	1
Corporate notes and bonds	—	64	—	64
Asset-backed securities	—	10	—	10
Municipal notes and bonds	—	5	—	5
Total long-term investments	2	85	—	87
Foreign exchange contracts	—	4	—	4
Total assets at fair value	\$ 1,383	\$ 258	\$ —	\$ 1,641
Liabilities:				
Foreign exchange contracts	\$ —	\$ 178	\$ —	\$ 178
Exchange option	—	—	1	1
Total liabilities at fair value	\$ —	\$ 178	\$ 1	\$ 179

WESTERN DIGITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
(Unaudited)

	July 1, 2016			
	Level 1	Level 2	Level 3	Total
	<i>(in millions)</i>			
Assets:				
Cash equivalents:				
Money market funds	\$ 2,199	\$ —	\$ —	\$ 2,199
Certificates of deposit	—	1	—	1
Total cash equivalents	<u>2,199</u>	<u>1</u>	<u>—</u>	<u>2,200</u>
Short-term investments:				
Certificates of deposit	—	202	—	202
Corporate notes and bonds	—	8	—	8
Asset-backed securities	—	11	—	11
Municipal notes and bonds	—	6	—	6
Total short-term investments	<u>—</u>	<u>227</u>	<u>—</u>	<u>227</u>
Long-term investments:				
U.S. Treasury securities	2	—	—	2
U.S. Government agency securities	—	10	—	10
International government securities	—	1	—	1
Corporate notes and bonds	—	89	—	89
Asset-backed securities	—	11	—	11
Municipal notes and bonds	—	6	—	6
Total long-term investments	<u>2</u>	<u>117</u>	<u>—</u>	<u>119</u>
Foreign exchange contracts	—	126	—	126
Call options	—	—	71	71
Total assets at fair value	<u>\$ 2,201</u>	<u>\$ 471</u>	<u>\$ 71</u>	<u>\$ 2,743</u>
Liabilities:				
Foreign exchange contracts	\$ —	\$ 23	\$ —	\$ 23
Exchange option	—	—	155	155
Total liabilities at fair value	<u>\$ —</u>	<u>\$ 23</u>	<u>\$ 155</u>	<u>\$ 178</u>

During the three and six months ended December 30, 2016 and January 1, 2016, the Company had no transfers of financial assets and liabilities between Level 1 and Level 2.

Assets and Liabilities Measured at Fair Value on a Recurring Basis Using Significant Unobservable Inputs (Level 3)

The fair value measurement of the call options and exchange options arising from the Company's Convertible Notes (as defined in Note 6 to the condensed consolidated financial statements) which are not actively traded, is determined using unobservable inputs (Level 3). These inputs include (i) the estimated amount and timing of settlement of the underlying debt; (ii) the probability of the achievement of the factor(s) on which the settlement is based; (iii) the risk-adjusted discount rate based on the expected term to maturity of the debt; and (iv) the economic incentive for holders to exercise their exchange option. Significant increases or decreases in any of those inputs in isolation could result in a significantly lower or higher fair value measurement.

There were no transfers of call options or exchange options out of Level 3 for the three and six months ended December 30, 2016.

WESTERN DIGITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
(Unaudited)

The following is a reconciliation of the call options reported in Other current assets and Other non-current assets in the Company's condensed consolidated balance sheet as of December 30, 2016 .

	<u>2017 Call Options</u>	<u>2020 Call Options</u>	<u>Total</u>
	<i>(in millions)</i>		
Fair value at July 1, 2016	\$ 70	\$ 1	\$ 71
Net realized loss	—	(1)	(1)
Redemptions	(70)	—	(70)
Fair value at December 30, 2016	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>

The following is a reconciliation of the exchange options reported in Accrued expenses and Other liabilities in the Company's condensed consolidated balance sheet as of December 30, 2016 .

	<u>2017 Exchange Options</u>	<u>2020 Exchange Options</u>	<u>Total</u>
	<i>(in millions)</i>		
Fair value at July 1, 2016	\$ 87	\$ 68	\$ 155
Net realized gain	(3)	(31)	(34)
Redemptions	(83)	(46)	(129)
Net unrealized loss	—	9	9
Fair value at December 30, 2016	<u>\$ 1</u>	<u>\$ —</u>	<u>\$ 1</u>

Financial Instruments Not Carried at Fair Value

For financial instruments where the carrying value (which includes principal adjusted for any unamortized issuance costs, and discounts or premiums) differs from fair value (which is based on quoted market prices), the following table represents the related carrying value and fair value for each of the Company's outstanding financial instruments. Each of the financial instruments presented below was categorized as Level 2 for all periods presented, based on the frequency of trading immediately prior to the end of the second quarter of 2017 and the fourth quarter of 2016 , respectively.

	<u>December 30, 2016</u>		<u>July 1, 2016</u>	
	<u>Carrying Value</u>	<u>Fair Value</u>	<u>Carrying Value</u>	<u>Fair Value</u>
	<i>(in millions)</i>			
Secured Notes	\$ 1,831	\$ 2,093	\$ 1,828	\$ 2,044
Unsecured Notes	3,237	3,978	3,229	3,575
Term Loan A	4,068	4,120	4,061	4,161
U.S. Term Loan B	—	—	3,546	3,773
U.S. Term Loan B-1	2,980	3,028	—	—
Euro Term Loan B ⁽¹⁾	—	—	960	981
Euro Term Loan B-1 ⁽¹⁾	927	946	—	—
Bridge Loan	—	—	2,995	3,000
Convertible Debt 2017	—	—	124	125
Convertible Debt 2020	30	31	251	264
Total	<u>\$ 13,073</u>	<u>\$ 14,196</u>	<u>\$ 16,994</u>	<u>\$ 17,923</u>

⁽¹⁾ Euro Term Loan B and Euro Term Loan B-1 outstanding principal amounts as of December 30, 2016 and July 1, 2016 were based upon the Euro to U.S. dollar exchange rate as of those respective dates.

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Cost Method Investments

From time to time, the Company enters into certain strategic investments for the promotion of business and strategic objectives. As of December 30, 2016 and July 1, 2016, the Company had aggregate net investments under the cost method of accounting of \$139 million and \$135 million, respectively, and these investments consisted of privately-held equity securities without a readily determinable fair value. The Company has determined that it is not practicable to estimate the fair value of these investments. These privately-held equity investments are reported under Other non-current assets in the condensed consolidated balance sheets.

Available-for-Sale Securities

The cost basis of the Company's investments classified as available-for-sale securities, individually and in the aggregate, approximated its fair value as of December 30, 2016 and January 1, 2016.

The cost basis and fair value of the Company's investments classified as available-for-sale securities as of December 30, 2016, by remaining contractual maturity, were as follows:

	Cost Basis	Fair Value
<i>(in millions)</i>		
Due in less than one year (short-term investments)	\$ 161	\$ 161
Due in one to five years (included in other non-current assets)	88	87
Total	\$ 249	\$ 248

The Company determined available-for-sale securities had no material other-than-temporary impairments in the three and six months ended December 30, 2016.

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Note 5. Derivatives

The majority of the Company's transactions are in U.S. dollars; however, some transactions are based in various foreign currencies. The Company purchases short-term, foreign exchange forward contracts to hedge the impact of foreign currency exchange fluctuations on certain underlying assets, liabilities and commitments for operating expenses and product costs denominated in foreign currencies. The purpose of entering into these hedging transactions is to minimize the impact of foreign currency fluctuations on the Company's results of operations. These contract maturity dates do not exceed 12 months. All foreign exchange forward contracts are for risk management purposes only. The Company does not purchase foreign exchange forward contracts for speculative or trading purposes. As of December 30, 2016, the Company had outstanding foreign exchange forward contracts with commercial banks for British pound sterling, Euro, Japanese yen, Malaysian ringgit, Philippine peso, Singapore dollar and Thai baht, which were designated as either cash flow or fair value hedges.

If the derivative is designated as a cash flow hedge, the effective portion of the change in fair value of the derivative is initially deferred in AOCI, net of tax. These amounts are subsequently recognized into earnings when the underlying cash flow being hedged is recognized into earnings. Recognized gains and losses on foreign exchange forward contracts entered into for manufacturing-related activities are reported in cost of revenue and presented within cash flow from operations. Hedge effectiveness is measured by comparing the hedging instrument's cumulative change in fair value from inception to maturity to the underlying exposure's terminal value. The Company determined the ineffectiveness associated with its cash flow hedges to be immaterial to the condensed consolidated financial statements for the three and six months ended December 30, 2016 and January 1, 2016.

A change in the fair value of fair value hedges is recognized in earnings in the period incurred and is reported as a component of cost of revenue or operating expenses, depending on the nature of the underlying hedged item. All fair value hedges were determined to be effective as of December 30, 2016 and July 1, 2016. The changes in fair value on these contracts were immaterial to the condensed consolidated financial statements during the three and six months ended December 30, 2016 and January 1, 2016.

As of December 30, 2016, the net amount of unrealized gains with respect to the Company's foreign exchange forward contracts that is expected to be reclassified into earnings within the next 12 months was \$65 million. In addition, as of December 30, 2016, the Company did not have any foreign exchange forward contracts with credit-risk-related contingent features.

See Note 4 to the condensed consolidated financial statements for additional disclosures related to the fair value of the Company's foreign exchange forward contracts.

Derivative Instruments

The fair value and balance sheet location of the Company's derivative instruments were as follows:

	Derivative Assets Reported in			
	Other Current Assets		Other Non-current Assets	
	December 30, 2016	July 1, 2016	December 30, 2016	July 1, 2016
	<i>(in millions)</i>			
Foreign exchange forward contracts designated	\$ 2	\$ 114	\$ —	\$ —
Foreign exchange forward contracts not designated	2	12	—	—
Call options	—	70	—	1
Total derivatives	<u>\$ 4</u>	<u>\$ 196</u>	<u>\$ —</u>	<u>\$ 1</u>

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	Derivative Liabilities Reported in			
	Accrued Expenses		Other Liabilities	
	December 30, 2016	July 1, 2016	December 30, 2016	July 1, 2016
	<i>(in millions)</i>			
Foreign exchange forward contracts designated	\$ 167	\$ 23	\$ —	\$ —
Foreign exchange forward contracts not designated	11	—	—	—
Exchange option	1	141	—	14
Total derivatives	<u>\$ 179</u>	<u>\$ 164</u>	<u>\$ —</u>	<u>\$ 14</u>

Netting Arrangements

The following table presents the gross amounts of the Company's derivative instruments, amounts offset due to master netting arrangements with the Company's various counterparties and the net amounts recognized in the condensed consolidated balance sheet as of December 30, 2016 :

Derivatives Designated as Hedging Instruments	Gross Amounts of Recognized Assets (Liabilities)	Gross Amounts Offset in the Balance Sheet	Net Amounts of Assets (Liabilities) Presented in the Balance Sheet	Gross Amounts Not Offset in the Balance Sheet		Net Amount
				Financial Instruments	Cash Collateral Received or Pledged	
	<i>(in millions)</i>					
Foreign exchange forward contracts:						
Financial assets	\$ 2	\$ —	\$ 2	\$ —	\$ —	\$ 2
Financial liabilities	(167)	—	(167)	—	—	(167)
Total derivative instruments	<u>\$ (165)</u>	<u>\$ —</u>	<u>\$ (165)</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ (165)</u>

The Company had a gross and net asset of \$118 million and \$114 million , respectively, and a gross and net liability of \$27 million and \$23 million , respectively, related to its derivative instruments outstanding as of July 1, 2016 .

Effect of Foreign Exchange Forward Contracts on the Condensed Consolidated Statements of Operations

The impact of foreign exchange forward contracts on the consolidated financial statements was as follows:

Derivatives in Cash Flow Hedging Relationships	Three Months Ended			
	Amount of Gain (Loss) Recognized in AOCI on Derivatives		Amount of Gain (Loss) Reclassified from AOCI into Earnings	
	December 30, 2016	January 1, 2016	December 30, 2016	January 1, 2016
	<i>(in millions)</i>			
Foreign exchange forward contracts	\$ (119)	\$ 13	\$ 16	\$ (25)

Derivatives in Cash Flow Hedging Relationships	Six Months Ended			
	Amount of Gain (Loss) Recognized in AOCI on Derivatives		Amount of Gain (Loss) Reclassified from AOCI into Earnings	
	December 30, 2016	January 1, 2016	December 30, 2016	January 1, 2016
	<i>(in millions)</i>			
Foreign exchange forward contracts	\$ (97)	\$ (40)	\$ 42	\$ (53)

The total net realized transaction and foreign exchange forward contract currency gains and losses were not material to the condensed consolidated financial statements for the three and six months ended December 30, 2016 and January 1, 2016 .

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
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Note 6. Debt

Debt consisted of the following as of December 30, 2016 and July 1, 2016 :

	December 30, 2016	July 1, 2016
	<i>(in millions)</i>	
Variable interest rate Term Loan A maturing 2021	\$ 4,125	\$ 4,125
Variable interest rate U.S. Term Loan B maturing 2023	—	3,750
Variable interest rate U.S. Term Loan B-1 maturing 2023	2,985	—
Variable interest rate Euro Term Loan B maturing 2023 ⁽¹⁾	—	987
Variable interest rate Euro Term Loan B-1 maturing 2023 ⁽¹⁾	929	—
7.375% senior secured notes due 2023	1,875	1,875
10.500% senior unsecured notes due 2024	3,350	3,350
Convertible senior notes	35	439
Bridge loans	—	3,000
Total debt	13,299	17,526
Issuance costs and debt discounts	(226)	(532)
Subtotal	13,073	16,994
Less bridge loans and current portion of long-term debt	(129)	(3,334)
Long-term debt	\$ 12,944	\$ 13,660

⁽¹⁾ Euro Term Loan B and Euro Term Loan B-1 outstanding principal amounts as of December 30, 2016 and July 1, 2016 were based upon the Euro to U.S. dollar exchange rate as of those respective dates.

Credit Agreement – Term Loans and Revolving Credit Facility

On April 29, 2016, the Company entered into a credit agreement (the “Credit Agreement”) that provided for a \$4.125 billion Term Loan A, a \$3.750 billion U.S. Term Loan B, a €885 million Euro Term Loan B and a \$1.0 billion revolving credit facility. The revolving credit facility includes a \$200 million sublimit for letters of credit.

In the first quarter ended September 30, 2016, the Company settled in full the principal amounts of the \$3.75 billion U.S. Term Loan B and the €885 million Euro Term Loan B, plus accrued interest. In connection with the settlement of the U.S. Term Loan B and Euro Term Loan B, the Company recognized a loss on debt extinguishment of \$227 million consisting of unamortized issuance costs and debt discount fees.

On August 17, 2016, the Company borrowed \$3.0 billion under a new U.S. dollar-denominated term loan (“U.S. Term Loan B-1”) under the Credit Agreement and used the proceeds of this new loan and cash of \$750 million to prepay in full the U.S. Term Loan B previously outstanding under the Credit Agreement. The U.S. Term Loan B-1 has an interest rate equal to, at the Company’s option, either an adjusted LIBOR rate, subject to a 0.75% floor, plus 3.75% or a base rate plus 2.75% (4.52% as of December 30, 2016). Principal payments on U.S. Term Loan B-1 of 0.25% are due quarterly and began on September 30, 2016 with the balance due on April 29, 2023. The U.S. Term Loan B-1 issuance costs of \$6 million are amortized to interest expense over the term of the loan. As of December 30, 2016, issuance costs of \$5 million remain unamortized.

On September 22, 2016, the Company borrowed €885 million under a new Euro-denominated term loan (“Euro Term Loan B-1”) under the Credit Agreement and used the proceeds of this new loan to prepay in full the Euro Term Loan B previously outstanding under the Credit Agreement. The Euro Term Loan B-1 has an interest rate equal to an adjusted EURIBOR rate, subject to a 0.75% floor, plus 3.25% (4.00% as of December 30, 2016). Principal payments on Euro Term Loan B-1 of 0.25% are due quarterly and began on September 30, 2016 with the balance due on April 29, 2023. The Euro Term Loan B-1 issuance costs of \$2 million are amortized to interest expense over the term of the loan. As of December 30, 2016, issuance costs of \$2 million remain unamortized.

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As of December 30, 2016, the revolving credit facility was not drawn upon, and there was no outstanding balance.

Beginning in September 2017, the Company is required to make quarterly principal payments on Term Loan A totaling \$206 million in 2018, \$309 million in 2019, \$413 million in 2020 and the remaining balance of \$3.197 billion due in 2021. As of December 30, 2016, Term Loan A had an outstanding balance of \$4.125 billion with a variable interest rate of 2.775%.

The obligations under the Credit Agreement are guaranteed by HGST, Inc., WD Media, LLC, Western Digital (Fremont), LLC and Western Digital Technologies, Inc. (“WDT”) (together referred to as the “WD Guarantors”), and are secured on a first-priority basis by a lien on substantially all the assets and properties of the Company and the WD Guarantors, including all of the capital stock held by these entities (subject to a 65% limitation on pledges of capital stock of foreign subsidiaries and domestic holding companies of foreign subsidiaries), subject to certain exceptions.

The term loans and the revolving credit loans under the Credit Agreement may be prepaid in whole or in part at any time without premium or penalty, subject to certain conditions, except that the U.S. Term Loan B-1 and the Euro Term Loan B-1 require the Company to pay a 1.0% prepayment fee if the loans thereunder are repaid in connection with certain “repricing” transactions on or before February 17, 2017, with respect to U.S. Term Loan B-1, and March 22, 2017, with respect to Euro Term Loan B-1.

The Credit Agreement requires the Company to comply with certain financial covenants, such as a leverage ratio and an interest coverage ratio. In addition, the documents governing substantially all of the Company’s outstanding debt, including the Credit Agreement, require the Company to comply with customary covenants that limit or restrict the Company’s and its subsidiaries’ ability to incur liens and indebtedness; make certain restricted payments, acquisitions, investments, loans and guarantees; and enter into certain transactions with affiliates, mergers and consolidations.

Additional Bridge Facility

On May 12, 2016, WDT entered into a short-term senior secured bridge credit agreement providing for \$3.0 billion in aggregate principal amount of senior secured bridge loans. On July 21, 2016, the Company repaid in full the \$3.0 billion aggregate principal amount outstanding, together with accrued interest.

Senior Notes

On April 13, 2016, the Company completed an offering of its \$1.875 billion aggregate principal amount of 7.375% senior secured notes due 2023 (the “Secured Notes”) and \$3.350 billion aggregate principal amount of 10.500% senior unsecured notes due 2024 (the “Initial Unsecured Notes”). On January 6, 2017, to fulfill the Company’s obligations under the registration rights agreement associated with the Initial Unsecured Notes, the Company commenced an exchange offer to exchange all of these outstanding unsecured notes for an equal principal amount of new 10.500% senior unsecured notes due 2024 (the “New Unsecured Notes”), with substantially the same terms as the Initial Unsecured Notes. The New Unsecured Notes are registered under the Securities Act of 1933, as amended, and have no transfer restrictions or rights to additional interest. On February 6, 2017, substantially all of the outstanding Initial Unsecured Notes were tendered in the exchange offer and accepted by the Company. The Initial Unsecured Notes, the New Unsecured Notes and the Secured Notes are collectively referred to as the “Notes”.

The Company is not required to make principal payments on the Notes prior to their respective maturity dates, except that the Company may be required to offer to purchase the Notes upon the occurrence of a change of control (as defined in the indentures governing the Notes) or with the proceeds of certain non-ordinary course asset sales. Interest payments on the Notes are due semi-annually in arrears.

The Notes are guaranteed by the WD Guarantors, and the Secured Notes and related guarantees are secured on an equal and ratable basis by liens on the same assets that secure indebtedness under the Credit Agreement.

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(Unaudited)

Convertible Notes, Exchange Options and Call Options

As of July 1, 2016, the Company had outstanding, through the acquisition of SanDisk, \$129 million aggregate principal amount of its 1.5% Convertible Senior Notes due 2017 (the “2017 Notes”) and \$310 million aggregate principal amount of its 0.5% Convertible Senior Notes due 2020 (the “2020 Notes”) and, together with the 2017 Notes, the “Convertible Notes”). The 2017 Notes mature on August 15, 2017 and the 2020 Notes mature on November 15, 2020.

During the three months ended December 30, 2016, the Company repurchased Convertible Notes for \$3 million of cash. During the six months ended December 30, 2016, the Company paid to the holders of the Convertible Notes for conversion and repurchase, \$493 million of cash and 0.3 million shares of the Company’s common stock with an aggregate value of \$16 million.

As of December 30, 2016, \$35 million principal amount of the 2020 Notes and an immaterial principal amount of the 2017 Notes were outstanding. For the 2020 Notes that remain outstanding, the conversion rate is 10.9006 units of reference property per \$1,000 principal amount of the 2020 Notes, corresponding to 2.6020 shares of the Company’s common stock and \$735.79 of cash, subject to adjustments under the indenture. The 2020 Notes are not currently exchangeable into reference property.

The Convertible Notes were bifurcated into a debt host and exchange option for accounting purposes. The exchange options are accounted for as a derivative liability because they are predominantly settled in cash. Changes in the fair value of the exchange options are reported, and will be reported until the Company extinguishes the related debt, in Other income (expense), net in the condensed consolidated statements of operations. The exchange options are measured and reported at fair value on a recurring basis, within Level 3 of the fair value hierarchy. The fair value of the unredeemed and unsettled exchange options was reported in Accrued expenses and Other liabilities in the condensed consolidated balance sheets. See Note 4 to the condensed consolidated financial statements for additional disclosures related to the fair values of the exchange options. For the three and six months ended December 30, 2016, the change in the fair value of the outstanding exchange options related to the Convertible Notes resulted in an immaterial gain.

In connection with the SanDisk acquisition, the Company assumed the outstanding call options entered into by SanDisk at the inception of the respective Convertible Notes, which were structured to reduce the potential economic dilution associated with the conversion of Convertible Notes. The call options are derivative instruments classified as an asset that result in the Company receiving cash and shares that partially offset the Company’s obligation upon conversion of the Convertible Notes. The fair value of the unredeemed and unsettled call options was reported in Other current assets and Other non-current assets in the condensed consolidated balance sheets. During the six months ended December 30, 2016, under the call options, the Company received \$61 million of cash and 0.1 million shares of the Company’s common stock which had an aggregate value of \$11 million. During the three and six months ended December 30, 2016, the Company recognized an immaterial non-cash loss related to the change in value in the outstanding call options. The value of the call options as of December 30, 2016 was immaterial.

The exchange and repurchase of the Convertible Notes and related settlement of the call options during the three and six months ended December 30, 2016 resulted in an immaterial net loss.

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Note 7. Pension and Other Post-Retirement Benefit Plans

The Company has pension and other post-retirement benefit plans in various countries. The Company's principal pension plans are in Japan. All pension and other post-retirement benefit plans outside of the Company's Japanese defined benefit pension plan (the "Japanese Plan") are immaterial to the Company's condensed consolidated financial statements. The expected long-term rate of return on the Japanese Plan assets is 2.5%.

Obligations and Funded Status

The following table presents the unfunded status of the benefit obligations for the Japanese Plan were as follows:

	December 30, 2016	July 1, 2016
	<i>(in millions)</i>	
Benefit obligations	\$ 281	\$ 326
Fair value of plan assets	190	212
Unfunded status	<u>\$ 91</u>	<u>\$ 114</u>

The following table presents the unfunded amounts related to the Japanese Plan as recognized on the Company's condensed consolidated balance sheets:

	December 30, 2016	July 1, 2016
	<i>(in millions)</i>	
Non-current liabilities	\$ 91	\$ 114
Net amount recognized	<u>\$ 91</u>	<u>\$ 114</u>

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(Unaudited)

Note 8 . Commitments, Contingencies and Related Parties*Flash Ventures*

The Company's business ventures with Toshiba Corporation ("Toshiba") consist of three separate legal entities: Flash Partners Ltd. ("Flash Partners"), Flash Alliance Ltd. ("Flash Alliance") and Flash Forward Ltd ("Flash Forward" and together with Flash Partners and Flash Alliance, referred to as "Flash Ventures"). The Company has a 49.9% ownership interest and Toshiba has a 50.1% ownership interest in each of these entities. Through Flash Ventures, the Company and Toshiba collaborate in the development and manufacture of NAND flash memory products, which are manufactured by Toshiba at its wafer fabrication facilities located in Yokkaichi, Japan, using semiconductor manufacturing equipment individually owned or leased by each Flash Ventures entity. The entities within Flash Ventures purchase wafers from Toshiba at cost and then resell those wafers to the Company and Toshiba at cost plus a markup.

The Company accounts for its ownership position of each entity with Flash Ventures under the equity method of accounting. The financial and other support provided by the Company in all periods presented was either contractually required or the result of a joint decision to expand wafer capacity, transition to new technologies or refinance existing equipment lease commitments. Entities within Flash Ventures are variable interest entities ("VIEs"). The Company evaluated whether it is the primary beneficiary of any of the entities within Flash Ventures for all periods presented and determined that it is not the primary beneficiary of any of the entities within Flash Ventures because it does not have a controlling financial interest in any of those entities. In determining whether the Company is the primary beneficiary, the Company analyzed the primary purpose and design of Flash Ventures, the activities that most significantly impact Flash Ventures' economic performance, and whether the Company had the power to direct those activities. The Company concluded, based upon its 49.9% ownership, the voting structure and the manner in which the day-to-day operations are conducted for each entity within Flash Ventures, that the Company lacked the power to direct most of the activities that most significantly impact the economic performance of each entity within Flash Ventures.

The following table presents the notes receivable from, and equity investments in, Flash Ventures as of December 30, 2016 and July 1, 2016 :

	December 30, 2016	July 1, 2016
	<i>(in millions)</i>	
Notes receivable, Flash Partners	\$ 145	\$ 65
Notes receivable, Flash Alliance	138	235
Notes receivable, Flash Forward	248	263
Investment in Flash Partners	178	202
Investment in Flash Alliance	267	306
Investment in Flash Forward	106	100
Total notes receivable and investments in Flash Ventures	\$ 1,082	\$ 1,171

During the three and six months ended December 30, 2016 , the Company made net payments to Flash Ventures of \$766 million and \$1.5 billion , respectively, for purchased NAND flash memory wafers and net loans and investments.

The Company makes, or will make, loans to Flash Ventures to fund equipment investments for new process technologies and additional wafer capacity. The Company aggregates its Flash Ventures' notes receivable into one class of financing receivables due to the similar ownership interest and common structure in each Flash Venture entity. For all reporting periods presented, no loans were past due and no loan impairments were recorded. The Company's notes receivable from each Flash Ventures entity, denominated in Japanese yen, are secured by equipment owned by that Flash Ventures entity.

The Company assesses financing receivable credit quality through financial and operational reviews of the borrower and creditworthiness, including credit rating agency ratings, of significant investors of the borrower, where material or known. Impairments, when required for credit worthiness, are recorded in Other income (expense), net in the condensed consolidated statements of operations.

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As of December 30, 2016 and July 1, 2016, the Company had accounts payable balances due to Flash Ventures of \$175 million and \$168 million, respectively.

The Company's maximum reasonably estimable loss exposure (excluding lost profits) as a result of its involvement with Flash Ventures, based upon the Japanese yen to U.S. dollar exchange rate at December 30, 2016, is presented below. Investments in Flash Ventures are denominated in Japanese yen and the maximum possible loss exposure excludes any cumulative translation adjustment due to revaluation from the Japanese yen to the U.S. dollar.

	December 30, 2016
	<i>(in millions)</i>
Notes receivable	\$ 531
Equity investments	551
Operating lease guarantees	1,102
Prepayments	26
Maximum estimable loss exposure	<u>\$ 2,210</u>

The Company is committed to purchase its provided three-month forecast of Flash Ventures' NAND wafer supply, which generally equals 50% of Flash Ventures' output. The Company is not able to estimate its total wafer purchase commitment obligation beyond its rolling three-month purchase commitment because the price is determined by reference to the future cost of producing the semiconductor wafers. In addition, the Company is committed to fund 49.9% to 50.0% of each Flash Ventures entity's investments to the extent that each Flash Ventures entity's operating cash flow is insufficient to fund these investments.

Off-Balance Sheet Liabilities

Flash Ventures sells and leases back from a consortium of financial institutions a portion of its tools and has entered into equipment lease agreements of which the Company guarantees half of the total outstanding obligations. The lease agreements contain customary covenants for Japanese lease facilities. In addition to containing customary events of default related to Flash Ventures that could result in an acceleration of Flash Ventures' obligations, the lease agreements contain acceleration clauses for certain events of default related to the guarantors, including the Company.

The following table presents the Company's portion of the remaining guarantee obligations under the Flash Ventures' lease facilities in both Japanese yen and U.S. dollar-equivalent based upon the Japanese yen to U.S. dollar exchange rate as of December 30, 2016.

	Lease Amounts	
	<i>(Japanese yen, in billions)</i>	<i>(U.S. dollar, in millions)</i>
Total guarantee obligations	¥ 129	\$ 1,102

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
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The following table details the breakdown of the Company's remaining guarantee obligations between the principal amortization and the purchase option exercise price at the end of the term of the Flash Ventures lease agreements, in annual installments as of December 30, 2016 in U.S. dollars based upon the Japanese yen to U.S. dollar exchange rate as of December 30, 2016 :

Annual Installments	Payment of Principal Amortization	Purchase Option Exercise Price at Final Lease Terms	Guarantee Amount
	<i>(in millions)</i>		
Year 1	\$ 269	\$ 47	\$ 316
Year 2	230	—	230
Year 3	184	71	255
Year 4	108	58	166
Year 5	33	102	135
Total guarantee obligations	<u>\$ 824</u>	<u>\$ 278</u>	<u>\$ 1,102</u>

The Company and Toshiba have agreed to mutually contribute to, and indemnify each other and Flash Ventures for, environmental remediation costs or liability resulting from Flash Ventures' manufacturing operations in certain circumstances. The Company has not made any indemnification payments, nor recorded any indemnification receivables, under any such agreements. As of December 30, 2016, no amounts have been accrued in the consolidated financial statements with respect to these indemnification guarantees.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
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Note 9. Shareholders' Equity*Stock-based Compensation Expense*

The following tables present the Company's stock-based compensation for equity-settled awards and related tax benefit by type and financial statement line included in the Company's condensed consolidated statements of operations:

	Three Months Ended		Six Months Ended	
	December 30, 2016	January 1, 2016	December 30, 2016	January 1, 2016
	<i>(in millions)</i>			
Options	\$ 11	\$ 12	\$ 23	\$ 26
Employee stock purchase plan	1	1	9	6
Restricted stock units ⁽¹⁾	90	24	169	47
Subtotal	102	37	201	79
Tax benefit	(29)	(10)	(54)	(20)
Total	<u>\$ 73</u>	<u>\$ 27</u>	<u>\$ 147</u>	<u>\$ 59</u>

⁽¹⁾ Restricted stock units ("RSUs") include performance stock units ("PSUs")

	Three Months Ended		Six Months Ended	
	December 30, 2016	January 1, 2016	December 30, 2016	January 1, 2016
	<i>(in millions)</i>			
Cost of revenue	\$ 11	\$ 4	\$ 24	\$ 9
Research and development	43	15	87	30
Selling, general and administrative	43	18	85	40
Restructuring	5	—	5	—
Subtotal	102	37	201	79
Tax benefit	(29)	(10)	(54)	(20)
Total	<u>\$ 73</u>	<u>\$ 27</u>	<u>\$ 147</u>	<u>\$ 59</u>

As of December 30, 2016, total compensation cost related to unvested stock options was \$83 million and will be amortized on a straight-line basis over a weighted average service period of approximately 2.8 years. As of December 30, 2016, total compensation cost related to the Company's Employee Stock Purchase Plan ("ESPP") rights issued to employees but not yet recognized was \$41 million and will be amortized on a straight-line basis over a weighted average service period of approximately 1.4 years.

As of December 30, 2016, the aggregate unamortized fair value of all unvested RSUs and PSUs was \$611 million, which will be recognized on a straight-line basis over a weighted average vesting period of approximately 2.6 years, assuming the performance metrics are met for the PSUs.

WESTERN DIGITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
(Unaudited)

Stock Option Activity

The following table summarizes stock option activity under the Company's incentive plans:

	<u>Number of Shares</u> <i>(in millions)</i>	<u>Weighted Average Exercise Price Per Share</u>	<u>Weighted Average Remaining Contractual Life</u> <i>(in years)</i>	<u>Aggregate Intrinsic Value</u> <i>(in millions)</i>
Options outstanding at July 1, 2016	9.0	\$ 55.74	3.9	\$ 60
Granted	2.8	44.83		
Exercised	(1.5)	34.56		
Canceled or expired	(0.6)	69.91		
Options outstanding at December 30, 2016	<u>9.7</u>	<u>54.86</u>	<u>4.4</u>	<u>187</u>
Exercisable at December 30, 2016	<u>4.8</u>	<u>53.61</u>	<u>2.8</u>	<u>101</u>
Vested and expected to vest after December 30, 2016	<u>9.4</u>	<u>55.00</u>	<u>4.3</u>	<u>180</u>

As of December 30, 2016, the Company had options outstanding to purchase an aggregate of 6.6 million shares with an exercise price below the quoted price of the Company's stock on that date resulting in an aggregate intrinsic value of \$187 million at that date.

RSU and PSU Activity

The following table summarizes RSU and PSU activity under the Company's incentive plans:

	<u>Number of Shares</u> <i>(in millions)</i>	<u>Weighted Average Grant Date Fair Value</u>
RSUs and PSUs outstanding at July 1, 2016	15.7	\$ 41.92
Granted	5.5	45.23
Vested	(2.3)	62.49
Forfeited	(1.4)	44.06
RSUs and PSUs outstanding at December 30, 2016	<u>17.5</u>	<u>42.82</u>
Expected to vest after December 30, 2016	<u>16.3</u>	<u>42.83</u>

RSUs and PSUs are generally settled in an equal number of shares of the Company's common stock at the time of vesting of the units. The aggregate value of RSUs and PSUs that became fully-vested during the six months ended December 30, 2016 was \$117 million, determined as of the vest date.

WESTERN DIGITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
(Unaudited)

SARs Activity

As of December 30, 2016, all outstanding stock appreciation rights (“SARs”) issued to employees were fully vested and will be settled in cash upon exercise. The fair value of SARs is solely subject to market price fluctuations. The following table presents the adjustments to the fair market value of SARs for the three and six months ended December 30, 2016 and January 1, 2016 :

	Three Months Ended		Six Months Ended	
	December 30, 2016	January 1, 2016	December 30, 2016	January 1, 2016
	<i>(in millions)</i>			
SAR expense (benefit)	\$ 3	\$ (10)	\$ 8	\$ (11)
Tax expense (benefit)	(1)	1	(2)	1
Total SAR expense (benefit)	\$ 2	\$ (9)	\$ 6	\$ (10)

The Company had a total liability of \$24 million and \$20 million related to SARs included in Accrued expenses in the Company’s condensed consolidated balance sheet as of December 30, 2016 and July 1, 2016, respectively. As of December 30, 2016, 0.4 million SARs were outstanding with a weighted average exercise price of \$7.99.

Stock Repurchase Program

The Company’s Board of Directors (the “Board”) has authorized \$5.0 billion for the repurchase of the Company’s common stock. The stock repurchase program is effective until February 3, 2020. The Company did not repurchase any shares of common stock during the three and six months ended December 30, 2016. The remaining amount available to be purchased under the Company’s stock repurchase program as of December 30, 2016 was \$2.1 billion.

Dividends to Shareholders

On September 13, 2012, the Company announced that the Board had authorized the adoption of a quarterly cash dividend policy. Under the cash dividend policy, holders of the Company’s common stock receive dividends when and as declared by the Board. The Company paid \$142 million in cash of dividends on July 15, 2016 relating to dividends declared on May 3, 2016 and paid \$143 million in cash of dividends on October 17, 2016 relating to dividends declared on August 3, 2016.

On November 3, 2016, the Board declared a cash dividend for the quarter ended December 30, 2016 of \$0.50 per share of the Company’s common stock, \$0.01 par value per share. The cash dividend of \$144 million was paid on January 17, 2017 to the Company’s shareholders of record as of December 30, 2016.

On February 1, 2017, the Board declared a cash dividend for the quarter ending March 31, 2017 of \$0.50 per share of the Company’s common stock, \$0.01 par value per share. The cash dividend will be paid on April 17, 2017 to shareholders of record as of March 31, 2017.

The Company may modify, suspend or cancel its cash dividend policy in any manner and at any time.

WESTERN DIGITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
(Unaudited)

Note 10 . Income Tax Expense (Benefit)

The following table presents the income tax expense (benefit) and the effective tax rate:

	Three Months Ended		Six Months Ended	
	December 30, 2016	January 1, 2016	December 30, 2016	January 1, 2016
	<i>(in millions)</i>			
Income tax expense (benefit)	\$ 86	\$ (7)	\$ 181	\$ 24
Effective tax rate	27%	(3)%	362%	4%

Income tax expense of \$181 million for the six months ended December 30, 2016 is attributable primarily to discrete effects consisting of income tax expense from the integration of SanDisk of \$90 million and a valuation allowance on acquired tax attributes of \$109 million . Income tax expense related to the SanDisk integration is partially offset by income tax benefit from deductible debt issuance costs, debt discounts and prepayment fees from the debt refinancing of \$96 million . These discrete items are the primary drivers of the effective tax rate for the six months ended December 30, 2016 .

The primary drivers for the difference between the effective tax rate for the three and six months ended December 30, 2016 and the U.S. Federal statutory rate of 35% are the current year generation of tax credits, tax holidays in Malaysia, the Philippines, Singapore and Thailand that expire at various dates from 2016 through 2029, for both periods, and the discrete items described above for the six months ended December 30, 2016 . For the three and six months ended January 1, 2016 , the difference between the effective tax rate and the U.S. Federal statutory rate of 35% is primarily due to tax holidays in Malaysia, the Philippines, Singapore and Thailand that expire at various dates from 2016 through 2029.

In the six months ended December 30, 2016 , the Company recorded a net decrease of \$14 million in its liability for unrecognized tax benefits. As of December 30, 2016 , the Company's liability for unrecognized tax benefits was approximately \$477 million . Accrued interest and penalties related to unrecognized tax benefits as of December 30, 2016 was \$84 million .

The Internal Revenue Service ("IRS") previously completed its field examination of the Company's federal income tax returns for fiscal years 2006 through 2009 and proposed certain adjustments. The Company received Revenue Agent Reports from the IRS that seek to increase the Company's U.S. taxable income which would result in additional federal tax expense totaling \$795 million , subject to interest. The issues in dispute relate primarily to transfer pricing with the Company's foreign subsidiaries and intercompany payable balances. The Company disagrees with the proposed adjustments and in September 2015, filed a protest with the IRS Appeals Office and received the IRS rebuttal in July 2016. The Company believes that its tax positions are properly supported and will vigorously contest the position taken by the IRS. In September 2015, the IRS commenced an examination of the Company's fiscal years 2010 through 2012.

The Company believes that adequate provision has been made for any adjustments that may result from tax examinations. However, the outcome of tax examinations cannot be predicted with certainty. If any issues addressed in the Company's tax examinations are resolved in a manner not consistent with management's expectations, the Company could be required to adjust its provision for income taxes in the period such resolution occurs. As of December 30, 2016 , it is not possible to estimate the amount of change, if any, in the unrecognized tax benefits that is reasonably possible within the next twelve months. Any significant change in the amount of the Company's liability for unrecognized tax benefits would most likely result from additional information or settlements relating to the examination of the Company's tax returns.

WESTERN DIGITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
(Unaudited)

Note 11 . Net Income (Loss) Per Common Share

The following table presents the computation of basic and diluted income (loss) per common share:

	Three Months Ended		Six Months Ended	
	December 30, 2016	January 1, 2016	December 30, 2016	January 1, 2016
	<i>(in millions, except per share data)</i>			
Net income (loss)	\$ 235	\$ 251	\$ (131)	\$ 534
Weighted average shares outstanding:				
Basic	286	232	285	231
Employee stock options, RSUs, PSUs, ESPP	8	2	—	3
Diluted	294	234	285	234
Income (loss) per common share				
Basic	\$ 0.82	\$ 1.08	\$ (0.46)	\$ 2.31
Diluted	\$ 0.80	\$ 1.07	\$ (0.46)	\$ 2.28
Anti-dilutive potential common shares excluded ⁽¹⁾	5	6	13	4

⁽¹⁾ For purposes of computing diluted income per common share, certain potentially dilutive securities have been excluded from the calculation because their effect would have been anti-dilutive.

The Company computes basic income per common share using net income and the weighted average number of common shares outstanding during the period. Diluted income per common share is computed using net income and the weighted average number of common shares and potentially dilutive common shares outstanding during the period. Potentially dilutive common shares include dilutive outstanding employee stock options, rights to purchase shares of common stock under the Company's ESPP, awards of RSUs and PSUs, and exchange options related to the Company's Convertible Notes .

WESTERN DIGITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
(Unaudited)

Note 12 . Acquisitions*Fiscal 2016 Acquisition*

In May 2016, the Company acquired SanDisk, a global leader in NAND flash storage solutions primarily to deepen the Company's expertise in non-volatile memory and enable the Company to vertically integrate into NAND, securing long-term access to solid state technology at a lower cost.

Assets Acquired and Liabilities Assumed at Fair Value

During the six months ended December 30, 2016, the Company increased goodwill by \$60 million due to an adjustment to the assessment of fair value for certain acquired intangible assets, inventory and property and equipment and a portion of the deferred tax liability. Management is continuing to assess the values assigned to the remaining assets acquired and liabilities assumed and may make further adjustments during the measurement period (through May 11, 2017) as further information becomes available. Any changes in the fair values of the assets acquired and liabilities assumed during the measurement period may result in adjustments to goodwill.

Pro Forma Financial Information

The financial information in the table below summarizes the combined results of operations for the Company and SanDisk, on a pro forma basis, as though the combination had occurred as of the beginning of 2016. The pro forma financial information for the periods presented includes the effects of adjustments related to amortization charges from acquired intangible assets, depreciation charges from acquired fixed assets, interest expenses from financing the acquisition, stock-based compensation expenses from the conversion of unvested equity awards and the elimination of certain expenses directly related to the transaction. The pro forma financial information as presented below is for informational purposes only and is not necessarily indicative of the results of operations that would have been achieved if the acquisition had taken place at the beginning of 2016.

	Three Months Ended	Six Months Ended
	January 1,	January 1,
	2016	2016
	<i>(in millions, except per share amounts)</i>	
Revenue, net	\$ 4,860	\$ 9,672
Net income	190	288
Basic income per common share	\$ 0.68	\$ 1.03
Diluted income per common share	\$ 0.67	\$ 1.01

WESTERN DIGITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
(Unaudited)

Note 13 . Employee Termination, Asset Impairment and Other Charges

The Company recorded the following charges related to employee terminations benefits, asset impairment and other charges:

	Three Months Ended		Six Months Ended	
	December 30, 2016	January 1, 2016	December 30, 2016	January 1, 2016
	<i>(in millions)</i>			
Employee termination and other charges:				
Restructuring Plan 2016	\$ 19	\$ —	\$ 46	\$ —
Closure of Foreign Manufacturing Facility	2	—	6	—
Business Realignment	7	27	44	75
Total employee termination and other charges	28	27	96	75
Stock-based compensation accelerations and adjustments				
Restructuring Plan 2016	—	—	(1)	—
Business Realignment	4	—	5	—
Total stock-based compensation accelerations and adjustments	4	—	4	—
Asset impairment:				
Closure of Foreign Manufacturing Facility	13	—	13	—
Business Realignment	—	—	—	8
Total asset impairment	13	—	13	8
Total employee termination and other charges, stock-based compensation adjustments and asset impairments	\$ 45	\$ 27	\$ 113	\$ 83

Restructuring Plan 2016

In 2016, the Company initiated a set of actions relating to the restructuring plan associated with the integration of substantial portions of its HGST and WD subsidiaries (“Restructuring Plan 2016”). Restructuring Plan 2016 consists of asset and footprint reduction, product road map consolidation and organization rationalization. In addition to the amounts recognized under Restructuring Plan 2016 for employee termination, asset impairments and other charges, as presented above, the Company recognized \$4 million and \$30 million in the three and six months ended December 30, 2016, respectively, of accelerated depreciation on facility assets in cost of revenue.

The following table presents an analysis of the components of the activity against the reserve during the six months ended December 30, 2016 :

	Employee Termination Benefits	Contract Termination and Other	Total
	<i>(in millions)</i>		
Accrual balance at July 1, 2016	\$ 26	\$ —	\$ 26
Charges	12	34	46
Cash payments	(30)	(32)	(62)
Accrual balance at December 30, 2016	\$ 8	\$ 2	\$ 10

WESTERN DIGITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
(Unaudited)

Closure of Foreign Manufacturing Facility

In January 2016, the Company announced the closing of its head component front end wafer manufacturing facility in Odawara, Japan, in order to reduce manufacturing costs. During the six months ended December 30, 2016, the Company recognized employee termination benefits and contract termination and other charges of \$6 million related to this closure. In addition, during the three months ended December 30, 2016, the Company recognized asset impairment charges of \$13 million related to this closure based on a current estimation of fair value. As of December 30, 2016, the Company substantially completed all activities related to the closure of the facility. The following table presents an analysis of the components of the activity against the reserve during the six months ended December 30, 2016:

	Employee Termination Benefits	Contract Termination and Other	Total
	<i>(in millions)</i>		
Accrual balance at July 1, 2016	\$ 14	\$ —	\$ 14
Charges	2	4	6
Cash payments	(15)	(7)	(22)
Non-cash items and other	(1)	3	2
Accrual balance at December 30, 2016	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>

Business Realignment

The Company periodically incurs charges as part of the integration process of recent acquisitions and to realign its operations with anticipated market demand. The following table presents an analysis of the components of the activity against the reserve during the six months ended December 30, 2016:

	Employee Termination Benefits	Contract Termination and Other	Total
	<i>(in millions)</i>		
Accrual balance at July 1, 2016	\$ 11	\$ 3	\$ 14
Charges	44	—	44
Cash payments	(51)	(1)	(52)
Non-cash items and other	6	—	6
Accrual balance at December 30, 2016	<u>\$ 10</u>	<u>\$ 2</u>	<u>\$ 12</u>

WESTERN DIGITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
(Unaudited)

Note 14 . Legal Proceedings

Unless otherwise stated below, for each of the matters described below, the Company has either recorded an accrual for losses that are probable and reasonably estimable or has determined that, while a loss is reasonably possible (including potential losses in excess of the amounts accrued by the Company), a reasonable estimate of the amount of loss or range of possible losses with respect to the claim or in excess of amounts already accrued by the Company cannot be made. The ability to predict the ultimate outcome of such matters involves judgments, estimates and inherent uncertainties. The actual outcome of such matters could differ materially from management's estimates.

Solely for purposes of this note, "WD" refers to Western Digital Corporation or one or more of its subsidiaries excluding HGST prior to the closing of the Company's acquisition of HGST on March 8, 2012 (the "HGST Closing Date") and SanDisk prior to the closing of the Company's acquisition of SanDisk on May 12, 2016 (the "SanDisk Closing Date"). HGST refers to Hitachi Global Storage Technologies Holdings Pte. Ltd. or one or more of its subsidiaries as of the HGST Closing Date, and SanDisk refers to SanDisk Corporation or one or more of its subsidiaries as of the SanDisk Closing Date and "the Company" refers to Western Digital Corporation and all of its subsidiaries on a consolidated basis including HGST and SanDisk.

Intellectual Property Litigation

In June 2008, Conville, Inc. ("Conville") filed a complaint with the U.S. District Court for the Eastern District of Texas against WD, HGST, and two other companies alleging infringement of U.S. Patent Nos. 6,314,473 and 4,916,635. The complaint sought unspecified monetary damages and injunctive relief. In October 2008, Conville amended its complaint to allege infringement of only the '473 patent. The '473 patent allegedly relates to interface technology to select between certain modes of a disk drive's operations relating to speed and noise. In July 2011, a verdict was rendered against WD and HGST in an amount that is not material to the Company's financial position, results of operations or cash flows, for which the Company previously recorded an accrual. In March 2015, WD and HGST filed notices of appeal with the U.S. District Court for the Federal Circuit ("Federal Circuit"). In April 2015, Conville filed a motion for reconsideration of the final judgment, and in May 2015, the Federal Circuit deactivated the appeal pending the District Court's decision on reconsideration. WD and HGST intend to continue to defend themselves vigorously in this matter.

In May 2016, Lambeth Magnetic Structures, LLC ("Lambeth") filed a complaint with the U.S. District Court for the Western District of Pennsylvania against WD and certain of its subsidiaries alleging infringement of U.S. Patent No. 7,128,988. The complaint seeks unspecified monetary damages and injunctive relief. The '988 patent, entitled "Magnetic Material Structures, Devices and Methods," allegedly relates to a magnetic material structure for hard disk drive devices. The Company intends to defend itself vigorously in this matter.

In December 2016, Memory Technologies, LLC ("MTL") filed two complaints – one with the International Trade Commission ("ITC") and the other with the U.S. District Court for the Central District of California – against WD and certain of its subsidiaries alleging infringement of various patents. In the ITC complaint, MTL asserts that certain of the Company's Secure Digital ("SD") and microSD products infringe U.S. Patent Nos. RE45,452; RE45,486; 7,464,469; 9,063,850; and 8,307,180. The ITC complaint seeks an exclusion order barring the accused products, and components thereof, from entry into the U.S. On January 5, 2017, the ITC issued a notice of institution of investigation regarding the complaint. On February 6, 2017, the Company filed its response to the complaint. In the other complaint, MTL asserts that certain of the Company's SD, microSD and/or eMMC products infringe the same patents asserted in the ITC complaint, as well as U.S. Patent Nos. 7,275,186; 7,827,370; and 7,739,487. The complaint seeks unspecified monetary damages. The Company intends to defend itself vigorously in these matters.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
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Antitrust

In June 2010, Ritz Camera & Image, LLC (“Ritz”) filed a complaint with the U.S. District Court for the Northern District of California, alleging that SanDisk violated federal antitrust laws by conspiring to monopolize and monopolizing the market for flash memory products. The lawsuit purports to be on behalf of direct purchasers of flash memory products sold by SanDisk and SanDisk-controlled joint ventures from June 2006 through the present. The complaint alleged that SanDisk created and maintained a monopoly by fraudulently obtaining patents and using them to restrain competition and by allegedly converting other patents for its competitive use. The complaint sought damages, injunctive relief, and fees and costs. In February 2011, the District Court granted in part SanDisk’s motion to dismiss, which resulted in Dr. Harari being dismissed as a defendant. Between 2013 and 2014, the District Court granted Ritz’s motion to substitute in as named plaintiff Albert Giuliano, the Chapter 7 Trustee of the Ritz bankruptcy estate, and the Trustee’s motions to add as named plaintiffs CPM Electronics Inc., E.S.E. Electronics, Inc. and Mflash, Inc. In May 2015, the District Court granted in part plaintiffs’ motion for class certification. In April 2016, the District Court granted SanDisk’s motion for summary judgment and entered judgment in SanDisk’s favor as to all of the plaintiffs’ claims. In May 2016, the plaintiffs filed a notice of appeal to the U.S. Court of Appeals for the Federal Circuit. The appeal is currently pending.

In July 2010, Samsung Electronics Co., Ltd. (“Samsung”) filed an action against Panasonic and SD-3C LLC (“SD-3C”) with the U.S. District Court for the Northern District of California, alleging that the defendants violated federal antitrust laws and California antitrust and unfair competition laws relating to the licensing practices and operations of SD-3C. The complaint seeks damages, restitution, injunctive and declaratory relief, and fees and costs. SanDisk is not a defendant in this case, but it established SD-3C along with Panasonic and Toshiba, and the complaint includes various factual allegations concerning SanDisk. As a member of SD-3C, SanDisk could be responsible for a portion of any monetary award. Other requested relief, if granted, could result in a loss of revenue to SanDisk. In August 2011, the District Court granted the defendants’ motion to dismiss, dismissing Samsung’s patent misuse claim with prejudice and all other claims with leave to amend. Samsung filed an amended complaint in September 2011. In January 2012, the District Court granted the defendants’ motion to dismiss Samsung’s amended complaint without leave to amend. Samsung appealed. In April 2014, the U.S. Court of Appeals for the Ninth Circuit reversed the District Court’s dismissal and remanded the case to the District Court for further proceedings. Samsung filed a third amended complaint in January 2015. In September 2015, the District Court granted in part the defendants’ motion to dismiss with leave to amend. In October 2015, Samsung filed a fourth amended complaint. In November 2015, the defendants filed a motion to dismiss. In September 2016, the District Court stayed the litigation pending the outcome of an ongoing arbitration between Samsung and Toshiba. The District Court denied the motion to dismiss without prejudice to refile after the stay is lifted.

In March 2011, a complaint was filed against SanDisk, SD-3C, Panasonic Corporation, Panasonic Corporation of North America, Toshiba and Toshiba America Electronic Components, Inc. with the U.S. District Court for the Northern District of California. The lawsuit purports to be on behalf of a nationwide class of indirect purchasers of SD cards. The complaint asserts claims under federal antitrust laws and California antitrust and unfair competition laws, as well as common law claims. The complaint seeks damages, restitution, injunctive relief, and fees and costs. The plaintiffs allege that the defendants conspired to artificially inflate the royalty costs associated with manufacturing SD cards, which in turn allegedly caused the plaintiffs to pay higher prices for SD cards. The allegations are similar to and incorporate allegations in Samsung Electronics Co., Ltd. v. Panasonic Corp., et al., described above. In May 2012, the District Court granted the defendants’ motion to dismiss the complaint with prejudice. The plaintiffs appealed. In May 2014, the U.S. Court of Appeals for the Ninth Circuit reversed the District Court’s dismissal and remanded the case to the District Court for further proceedings. In February 2015, the plaintiffs filed a second amended complaint in the District Court. In September 2015, the District Court granted the defendants’ motion to dismiss with leave to amend. In November 2015, the plaintiffs filed a third amended complaint. In November 2015, the defendants filed a motion to dismiss the plaintiffs’ federal law claims. In October 2016, the District Court granted the defendants’ motion with leave to amend and the defendants filed a motion to dismiss the plaintiffs’ remaining claims. Discovery is presently stayed until after completion of the pleading stage. The Company intends to defend itself vigorously in this matter.

Securities

Beginning in March 2015, SanDisk and two of its officers, Sanjay Mehrotra and Judy Bruner, were named in three putative class action lawsuits filed with the U.S. District Court for the Northern District of California. Two complaints are allegedly brought on behalf of a class of purchasers of SanDisk’s securities between October 2014 and March 2015, and one is brought on behalf of a purported class of purchasers of SanDisk’s securities between April 2014 and April 2015. The complaints

WESTERN DIGITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
(Unaudited)

generally allege violations of federal securities laws arising out of alleged misstatements or omissions by the defendants during the alleged class periods. The complaints seek, among other things, damages and fees and costs. In July 2015, the District Court consolidated the cases and appointed Union Asset Management Holding AG and KBC Asset Management NV as lead plaintiffs. The lead plaintiffs filed an amended complaint in August 2015. In January 2016, the District Court granted the defendants' motion to dismiss and dismissed the amended complaint with leave to amend. In February 2016, the District Court issued an order appointing as new lead plaintiffs Bristol Pension Fund; City of Milford, Connecticut Pension & Retirement Board; Pavers and Road Builders Pension, Annuity and Welfare Funds; the Newport News Employees' Retirement Fund; and Massachusetts Laborers' Pension Fund (collectively, the "Institutional Investor Group"). In March 2016, the Institutional Investor Group filed an amended complaint. The defendants filed a motion to dismiss in April 2016. In June 2016, the District Court granted the motion and dismissed the amended complaint with leave to amend. In July 2016, the Institutional Investor Group filed a further amended complaint. The defendants filed a motion to dismiss in August 2016. In January 2017, the District Court denied the motion to dismiss without prejudice to the defendants filing a renewed motion to dismiss, which the defendants filed soon thereafter. The Company intends to defend itself vigorously in this matter.

Other Matters

In December 2011, the German Central Organization for Private Copying Rights (Zentralstelle für private Überspielungsrechte) ("ZPÜ"), an organization consisting of several copyright collecting societies, instituted arbitration proceedings against WD's German subsidiary ("WD Germany") before the Copyright Arbitration Board ("CAB") claiming copyright levies for multimedia hard drives, external hard drives and network hard drives sold or introduced into commerce in Germany by WD Germany from January 2008 through December 2010. In February 2013, WD Germany filed a declaratory relief action against ZPÜ in the Higher Regional Court of Munich (the "Higher Court"), seeking an order from the Higher Court to determine the copyright levy issue. In May 2013, ZPÜ filed a counter-claim against WD Germany with the Higher Court, seeking copyright levies for multimedia hard drives, external hard drives and network hard drives sold or introduced into commerce from January 2008 through December 2010 based on tariffs published by ZPÜ in November 2011. In January 2015, the Higher Court ruled in favor of ZPÜ. In its ruling, the Higher Court declared that WD Germany must pay certain levies on certain products which it sold in Germany between January 2008 and December 2010. The judgment specifies levy amounts on certain products sold from January 2008 through December 2010 and directs WD Germany to provide applicable sales data to ZPÜ. The exact amount of the judgment has not been determined. ZPÜ and WD Germany filed appeals with the German Federal Court of Justice in February 2015. The Company intends to defend itself vigorously in this matter.

In December 2014, ZPÜ submitted a pleading to the CAB seeking copyright levies for multimedia hard drives, external hard drives and network hard drives sold or introduced into commerce in Germany by WD Germany between January 2012 and December 2013. The Company intends to defend itself vigorously in this matter.

The Company has recorded an accrual for German copyright levies in an amount that is not material to the Company's financial position, results of operations or cash flows. It is reasonably possible that the Company may incur losses totaling up to \$133 million, including the amounts accrued.

In the normal course of business, the Company is subject to other legal proceedings, lawsuits and other claims. Although the ultimate aggregate amount of probable monetary liability or financial impact with respect to these other matters is subject to many uncertainties, management believes that any monetary liability or financial impact to the Company from these other matters, individually and in the aggregate, would not be material to the Company's financial condition, results of operations or cash flows. However, any monetary liability and financial impact to the Company from these other matters could differ materially from the Company's expectations.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
(Unaudited)

Note 15 . Separate Financial Information of Guarantor Subsidiaries

The New Unsecured Notes are registered under the Securities Act of 1933, as amended, and have no transfer restrictions or rights to additional interest. The New Unsecured Notes are fully and unconditionally guaranteed, jointly and severally, on a senior unsecured basis, subject to certain customary guarantor release conditions, by the WD Guarantors (or the “Guarantor Subsidiaries”). The guarantee by a Guarantor Subsidiary will be released in the event of (i) the designation of a Guarantor Subsidiary as an unrestricted subsidiary under the indenture governing the New Unsecured Notes, (ii) the release of a Guarantor Subsidiary from its guarantee of indebtedness under the Credit Agreement or other indebtedness that would have required the Guarantor Subsidiary to guarantee the New Unsecured Notes, (iii) the sale, issuance or other disposition of capital stock of a Guarantor Subsidiary such that it is no longer a restricted subsidiary under the indenture governing the New Unsecured Notes, (iv) the sale of all or substantially all of a Guarantor Subsidiary’s assets, (v) the Company’s exercise of its defeasance options under the indenture governing the New Unsecured Notes, (vi) the dissolution or liquidation of a Guarantor Subsidiary or (vii) the sale of all the equity interest in a Guarantor Subsidiary. The Company’s other domestic subsidiaries and its foreign subsidiaries (collectively, the “Non-Guarantor Subsidiaries”) do not guarantee the New Unsecured Notes. The following condensed consolidating financial information reflects the summarized financial information of Western Digital Corporation (“Parent”), the Guarantor Subsidiaries on a combined basis, and the Non-Guarantor Subsidiaries on a combined basis.

For more information regarding the New Unsecured Notes, refer to Note 6 to the condensed consolidated financial statements.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
(Unaudited)

Condensed Consolidating Balance Sheet
As of December 30, 2016

	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Total Company
<i>(in millions)</i>					
ASSETS					
Current assets:					
Cash and cash equivalents	\$ 46	\$ 883	\$ 4,011	\$ —	\$ 4,940
Short-term investments	—	—	161	—	161
Accounts receivable, net	—	1,320	684	—	2,004
Intercompany receivable	813	1,878	2,923	(5,614)	—
Inventories	—	828	1,455	(198)	2,085
Other current assets	4	253	159	—	416
Total current assets	863	5,162	9,393	(5,812)	9,606
Property, plant and equipment, net	—	1,207	2,031	—	3,238
Notes receivable and investments in Flash Ventures	—	—	1,082	—	1,082
Goodwill	—	325	9,680	—	10,005
Other intangible assets, net	—	19	4,450	—	4,469
Investments in consolidated subsidiaries	17,942	17,874	—	(35,816)	—
Loans due from consolidated affiliates	5,230	15	—	(5,245)	—
Other non-current assets	46	99	466	(36)	575
Total assets	\$ 24,081	\$ 24,701	\$ 27,102	\$ (46,909)	\$ 28,975
LIABILITIES AND SHAREHOLDERS' EQUITY					
Current liabilities:					
Accounts payable	\$ —	\$ 225	\$ 1,787	\$ —	\$ 2,012
Intercompany payable	180	4,823	611	(5,614)	—
Accounts payable to related parties	—	—	175	—	175
Accrued expenses	126	507	368	—	1,001
Accrued compensation	—	376	205	—	581
Accrued warranty	—	4	186	—	190
Current portion of long-term debt	129	—	—	—	129
Total current liabilities	435	5,935	3,332	(5,614)	4,088
Long-term debt	12,915	—	29	—	12,944
Loans due to consolidated affiliates	—	34	5,211	(5,245)	—
Other liabilities	—	670	578	(37)	1,211
Total liabilities	13,350	6,639	9,150	(10,896)	18,243
Shareholders' equity	10,731	18,062	17,952	(36,013)	10,732
Total liabilities and shareholders' equity	\$ 24,081	\$ 24,701	\$ 27,102	\$ (46,909)	\$ 28,975

WESTERN DIGITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
(Unaudited)

Condensed Consolidating Balance Sheet
As of July 1, 2016

	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Total Company
<i>(in millions)</i>					
ASSETS					
Current assets:					
Cash and cash equivalents	\$ —	\$ 1,206	\$ 6,945	\$ —	\$ 8,151
Short-term investments	—	—	227	—	227
Accounts receivable, net	—	985	476	—	1,461
Intercompany receivable	934	886	2,546	(4,366)	—
Inventories	—	896	1,450	(217)	2,129
Other current assets	4	276	379	(43)	616
Total current assets	938	4,249	12,023	(4,626)	12,584
Property, plant and equipment, net	—	1,265	2,238	—	3,503
Notes receivable and investments in Flash Ventures	—	—	1,171	—	1,171
Goodwill	—	324	9,627	—	9,951
Other intangible assets, net	—	28	5,006	—	5,034
Investments in consolidated subsidiaries	18,009	27,020	—	(45,029)	—
Loans due from consolidated affiliates	6,000	55	—	(6,055)	—
Other non-current assets	50	33	702	(166)	619
Total assets	\$ 24,997	\$ 32,974	\$ 30,767	\$ (55,876)	\$ 32,862
LIABILITIES AND SHAREHOLDERS' EQUITY					
Current liabilities:					
Accounts payable	\$ —	\$ 239	\$ 1,649	\$ —	\$ 1,888
Intercompany payable	119	4,043	204	(4,366)	—
Accounts payable to related parties	—	—	168	—	168
Accrued expenses	109	462	404	20	995
Accrued compensation	—	222	170	—	392
Accrued warranty	—	4	168	—	172
Bridge loan	—	2,995	—	—	2,995
Current portion of long-term debt	14	—	325	—	339
Total current liabilities	242	7,965	3,088	(4,346)	6,949
Long-term debt	13,610	—	50	—	13,660
Loans due to consolidated affiliates	—	6,000	55	(6,055)	—
Other liabilities	—	862	475	(229)	1,108
Total liabilities	13,852	14,827	3,668	(10,630)	21,717
Shareholders' equity	11,145	18,147	27,099	(45,246)	11,145
Total liabilities and shareholders' equity	\$ 24,997	\$ 32,974	\$ 30,767	\$ (55,876)	\$ 32,862

WESTERN DIGITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
(Unaudited)

Condensed Consolidating Statements of Operations
For the three months ended December 30, 2016

	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Total Company
	<i>(in millions)</i>				
Revenue, net	\$ —	\$ 3,786	\$ 4,245	\$ (3,143)	\$ 4,888
Cost of revenue	—	3,085	3,495	(3,225)	3,355
Gross profit	—	701	750	82	1,533
Operating expenses:					
Research and development	—	372	213	—	585
Selling, general and administrative	3	252	103	—	358
Intercompany operating expense (income)	—	(218)	218	—	—
Employee termination, asset impairment and other charges	—	9	36	—	45
Total operating expenses	3	415	570	—	988
Operating income (loss)	(3)	286	180	82	545
Interest and other income (expense):					
Interest income	86	—	2	(83)	5
Interest expense	(203)	—	(85)	83	(205)
Other expense, net	(2)	(5)	(17)	—	(24)
Total interest and other expense, net	(119)	(5)	(100)	—	(224)
Income (loss) before taxes	(122)	281	80	82	321
Income tax expense (benefit)	(87)	116	57	—	86
Equity in earnings from subsidiaries	270	19	—	(289)	—
Net income	\$ 235	\$ 184	\$ 23	\$ (207)	\$ 235

WESTERN DIGITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
(Unaudited)

Condensed Consolidating Statements of Operations
For the six months ended December 30, 2016

	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Total Company
	<i>(in millions)</i>				
Revenue, net	\$ —	\$ 7,484	\$ 8,538	\$ (6,420)	\$ 9,602
Cost of revenue	—	6,150	7,048	(6,464)	6,734
Gross profit	—	1,334	1,490	44	2,868
Operating expenses:					
Research and development	—	813	411	—	1,224
Selling, general and administrative	4	526	224	—	754
Intercompany operating expense (income)	—	(569)	569	—	—
Employee termination, asset impairment and other charges	—	58	55	—	113
Total operating expenses	4	828	1,259	—	2,091
Operating income (loss)	(4)	506	231	44	777
Interest and other income (expense):					
Interest income	180	1	9	(180)	10
Interest expense	(431)	(5)	(185)	180	(441)
Other expense, net	(274)	(4)	(18)	—	(296)
Total interest and other expense, net	(525)	(8)	(194)	—	(727)
Income (loss) before taxes	(529)	498	37	44	50
Income tax expense (benefit)	(181)	121	241	—	181
Equity in earnings from subsidiaries	217	(208)	—	(9)	—
Net income (loss)	\$ (131)	\$ 169	\$ (204)	\$ 35	\$ (131)

WESTERN DIGITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
(Unaudited)

Condensed Consolidating Statements of Operations
For the three months ended January 1, 2016

	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Total Company
	<i>(in millions)</i>				
Revenue, net	\$ —	\$ 3,411	\$ 3,611	\$ (3,705)	\$ 3,317
Cost of revenue	—	3,190	2,918	(3,697)	2,411
Gross profit	—	221	693	(8)	906
Operating expenses:					
Research and development	—	270	119	—	389
Selling, general and administrative	1	138	100	—	239
Intercompany operating expense (income)	—	(278)	278	—	—
Employee termination, asset impairment and other charges	—	20	7	—	27
Total operating expenses	1	150	504	—	655
Operating income (loss)	(1)	71	189	(8)	251
Interest and other income (expense):					
Interest income	—	—	4	1	5
Interest expense	—	(11)	(2)	—	(13)
Other income, net	—	—	2	(1)	1
Total interest and other income (expense), net	—	(11)	4	—	(7)
Income (loss) before taxes	(1)	60	193	(8)	244
Income tax expense (benefit)	—	19	(26)	—	(7)
Equity in earnings from subsidiaries	252	217	—	(469)	—
Net income	\$ 251	\$ 258	\$ 219	\$ (477)	\$ 251

WESTERN DIGITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
(Unaudited)

Condensed Consolidating Statements of Operations
For the six months ended January 1, 2016

	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Total Company
	<i>(in millions)</i>				
Revenue, net	\$ —	\$ 6,837	\$ 7,024	\$ (7,184)	\$ 6,677
Cost of revenue	—	6,410	5,578	(7,172)	4,816
Gross profit	—	427	1,446	(12)	1,861
Operating expenses:					
Research and development	—	579	195	—	774
Selling, general and administrative	2	309	120	—	431
Intercompany operating expense (income)	—	(590)	590	—	—
Employee termination, asset impairment and other charges	—	70	13	—	83
Total operating expenses	2	368	918	—	1,288
Operating income (loss)	(2)	59	528	(12)	573
Interest and other income (expense):					
Interest income	—	1	8	—	9
Interest expense	—	(22)	(4)	—	(26)
Other income, net	—	—	2	—	2
Total interest and other income (expense), net	—	(21)	6	—	(15)
Income (loss) before taxes	(2)	38	534	(12)	558
Income tax expense (benefit)	—	52	(28)	—	24
Equity in earnings from subsidiaries	536	562	—	(1,098)	—
Net income	\$ 534	\$ 548	\$ 562	\$ (1,110)	\$ 534

WESTERN DIGITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
(Unaudited)

Condensed Consolidating Statement of Comprehensive Income (Loss)
For the three months ended December 30, 2016

	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Total Company
	<i>(in millions)</i>				
Net income	\$ 235	\$ 184	\$ 23	\$ (207)	\$ 235
Other comprehensive loss, before tax:					
Actuarial pension gain	1	1	1	(2)	1
Foreign currency translation adjustment	(186)	(186)	(210)	396	(186)
Net unrealized loss on foreign exchange contracts	(136)	(136)	(132)	268	(136)
Total other comprehensive loss, before tax	(321)	(321)	(341)	662	(321)
Income tax benefit related to items of other comprehensive loss	9	10	9	(19)	9
Other comprehensive loss, net of tax	(312)	(311)	(332)	643	(312)
Total comprehensive loss	\$ (77)	\$ (127)	\$ (309)	\$ 436	\$ (77)

Condensed Consolidating Statement of Comprehensive Income (Loss)
For the six months ended December 30, 2016

	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Total Company
	<i>(in millions)</i>				
Net income (loss)	\$ (131)	\$ 169	\$ (204)	\$ 35	\$ (131)
Other comprehensive loss, before tax:					
Actuarial pension gain	6	6	6	(12)	6
Foreign currency translation adjustment	(169)	(169)	(192)	361	(169)
Net unrealized loss on foreign exchange contracts	(140)	(140)	(136)	276	(140)
Total other comprehensive loss, before tax	(303)	(303)	(322)	625	(303)
Income tax benefit related to items of other comprehensive loss	3	3	1	(4)	3
Other comprehensive loss, net of tax	(300)	(300)	(321)	621	(300)
Total comprehensive loss	\$ (431)	\$ (131)	\$ (525)	\$ 656	\$ (431)

WESTERN DIGITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
(Unaudited)

Condensed Consolidating Statement of Comprehensive Income (Loss)
For the three months ended January 1, 2016

	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Total Company
	<i>(in millions)</i>				
Net income	\$ 251	\$ 258	\$ 219	\$ (477)	\$ 251
Other comprehensive income, before tax:					
Net unrealized gain on foreign exchange contracts	38	38	29	(67)	38
Net unrealized loss on available-for-sale securities	(2)	(3)	(3)	6	(2)
Total other comprehensive income, before tax	36	35	26	(61)	36
Income tax benefit related to items of other comprehensive income	—	—	—	—	—
Other comprehensive income, net of tax	36	35	26	(61)	36
Total comprehensive income	<u>\$ 287</u>	<u>\$ 293</u>	<u>\$ 245</u>	<u>\$ (538)</u>	<u>\$ 287</u>

Condensed Consolidating Statement of Comprehensive Income (Loss)
For the six months ended January 1, 2016

	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Total Company
	<i>(in millions)</i>				
Net income	\$ 534	\$ 548	\$ 562	\$ (1,110)	\$ 534
Other comprehensive income, before tax:					
Net unrealized gain on foreign exchange contracts	13	13	12	(25)	13
Net unrealized loss on available-for-sale securities	(1)	(2)	(2)	4	(1)
Total other comprehensive income, before tax	12	11	10	(21)	12
Income tax benefit related to items of other comprehensive income	—	—	—	—	—
Other comprehensive income, net of tax	12	11	10	(21)	12
Total comprehensive income	<u>\$ 546</u>	<u>\$ 559</u>	<u>\$ 572</u>	<u>\$ (1,131)</u>	<u>\$ 546</u>

WESTERN DIGITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
(Unaudited)

Condensed Consolidating Statement of Cash Flows
For the six months ended December 30, 2016

	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Total Company
	<i>(in millions)</i>				
Cash flows from operating activities					
Net cash provided by (used in) operating activities	\$ (256)	\$ 211	\$ 1,443	\$ 102	\$ 1,500
Cash flows from investing activities					
Purchases of property, plant and equipment	—	(136)	(194)	—	(330)
Proceeds from the sale of equipment	—	—	1	—	1
Purchases of investments	—	—	(239)	—	(239)
Proceeds from sale of investments	—	—	55	—	55
Proceeds from maturities of investments	—	—	279	—	279
Investments in Flash Ventures	—	—	(20)	—	(20)
Notes receivable issuances to Flash Ventures	—	—	(309)	—	(309)
Notes receivable proceeds from Flash Ventures	—	—	259	—	259
Strategic investments and other, net	—	—	(12)	—	(12)
Intercompany loans to consolidated affiliates	770	40	—	(810)	—
Advances to consolidated affiliates	293	(285)	—	(8)	—
Net cash provided by (used in) investing activities	1,063	(381)	(180)	(818)	(316)
Cash flows from financing activities					
Issuance of stock under employee stock plans	90	—	—	—	90
Taxes paid on vested stock awards under employee stock plans	(40)	—	—	—	(40)
Excess tax benefits from employee stock plans	56	—	—	—	56
Proceeds from acquired call option	—	—	61	—	61
Dividends paid to shareholders	(284)	—	—	—	(284)
Repayment of debt	(4,767)	(2,995)	(492)	—	(8,254)
Proceeds from debt	3,992	—	—	—	3,992
Debt issuance costs	(7)	—	—	—	(7)
Intercompany loan from parent	—	(5,966)	5,156	810	—
Change in investment in consolidated subsidiaries	199	8,808	(8,913)	(94)	—
Net cash used in financing activities	(761)	(153)	(4,188)	716	(4,386)
Effect of exchange rate changes on cash	—	—	(9)	—	(9)
Net increase (decrease) in cash and cash equivalents	46	(323)	(2,934)	—	(3,211)
Cash and cash equivalents, beginning of year	—	1,206	6,945	—	8,151
Cash and cash equivalents, end of period	\$ 46	\$ 883	\$ 4,011	\$ —	\$ 4,940

WESTERN DIGITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)
(Unaudited)

Condensed Consolidating Statement of Cash Flows
For the six months ended January 1, 2016

	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Total Company
	<i>(in millions)</i>				
Cash flows from operating activities					
Net cash provided by operating activities	\$ 12	\$ 266	\$ 852	\$ 13	\$ 1,143
Cash flows from investing activities					
Purchases of property, plant and equipment	—	(114)	(186)	—	(300)
Purchases of investments	—	—	(408)	—	(408)
Proceeds from sale of investments	—	—	—	266	266
Proceeds from maturities of investments	—	—	266	(266)	—
Strategic investments and other, net	—	—	(12)	—	(12)
Advances from (to) consolidated affiliates	207	(207)	—	—	—
Net cash provided by (used in) investing activities	207	(321)	(340)	—	(454)
Cash flows from financing activities					
Issuance of stock under employee stock plans	54	—	—	—	54
Taxes paid on vested stock awards under employee stock plans	(44)	—	—	—	(44)
Excess tax benefits from employee stock plans	(6)	—	—	—	(6)
Repurchases of common stock	(60)	—	—	—	(60)
Dividends paid to shareholders	(231)	—	—	—	(231)
Repayment of debt	—	(63)	—	—	(63)
Change in investment in consolidated subsidiaries	68	(52)	(3)	(13)	—
Net cash used in financing activities	(219)	(115)	(3)	(13)	(350)
Net increase (decrease) in cash and cash equivalents	—	(170)	509	—	339
Cash and cash equivalents, beginning of year	—	661	4,363	—	5,024
Cash and cash equivalents, end of period	\$ —	\$ 491	\$ 4,872	\$ —	\$ 5,363

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

The following discussion and analysis contains forward-looking statements within the meaning of the federal securities laws, and should be read in conjunction with the disclosures we make concerning risks and other factors that may affect our business and operating results. You should read this information in conjunction with the unaudited condensed consolidated financial statements and the notes thereto included in this Quarterly Report on Form 10-Q, and the audited consolidated financial statements and notes thereto and Part II, Item 7, contained in our Annual Report on Form 10-K for the fiscal year ended July 1, 2016 .

Unless otherwise indicated, references herein to specific years and quarters are to our fiscal years and fiscal quarters. As used herein, the terms "we," "us," "our," and the "Company" refer to Western Digital Corporation and its subsidiaries.

Our Company

We are a leading developer, manufacturer and provider of data storage devices and solutions that address the evolving needs of the information technology ("IT") industry and the infrastructure that enables the proliferation of data in virtually every industry. Our broad portfolio of offerings addresses three categories: Data Center Devices and Solutions (capacity and performance enterprise hard disk drives ("HDD"), enterprise solid-state drives ("SSD"), data center software and system solutions); Client Devices (mobile, desktop, gaming and digital video hard drives, client SSDs, embedded products and wafers); and Client Solutions (removable products, hard drive content solutions and flash content solutions). We also generate license and royalty revenue related to our intellectual property which is included in each of the three categories.

Our fiscal year ends on the Friday nearest to June 30 and typically consists of 52 weeks. Fiscal years 2017 , which ends on June 30, 2017 , and 2016 , which ended July 1, 2016 , are both comprised of 52 weeks, with all quarters presented consisting of 13 weeks.

Recent Developments

Debt Facilities

During the first half of 2017, we settled certain debt facilities and entered into new debt facilities at lower rates. The financing arrangement activities during the first half of 2017 were:

- We paid in full, with accrued interest, our \$3.0 billion short-term senior secured bridge credit agreement.
- We settled our \$3.750 billion U.S. Term Loan B tranche with a new issuance of a \$3.0 billion six -year U.S. dollar-denominated term loan ("U.S. Term Loan B-1") at an interest rate lower than our U.S. Term Loan B tranche. Proceeds from this new loan and a voluntary cash prepayment of \$750 million were used to settle our U.S. Term Loan B tranche.
- We settled our €885 million Euro Term Loan B tranche with a new issuance of a €885 million seven -year Euro-denominated term loan ("Euro Term Loan B-1") at an interest rate lower than our Euro Term Loan B tranche.
- We paid to the holders of our Convertible Notes (as defined below), for conversion and repurchase, \$493 million of cash and 0.3 million shares of our common stock with an aggregate value of \$16 million . In conjunction with the settlements, we received from the exercise of the related call options, \$61 million of cash and 0.1 million shares of our common stock which had an aggregate value of \$11 million .

For additional information regarding our debt facilities, see Part I, Item 1, Note 6 , in this Quarterly Report on Form 10-Q .

Results of Operations

Second Quarter and First Half Overview

The following table sets forth, for the periods presented, selected summary information from our condensed consolidated statements of operations by dollars and percentage of net revenue:

	Three Months Ended						Six Months Ended					
	December 30, 2016		January 1, 2016		% Change	December 30, 2016		January 1, 2016		% Change		
<i>(in millions, except percentages)</i>												
Revenue, net	\$ 4,888	100.0%	\$ 3,317	100.0%	47 %	\$ 9,602	100.0 %	\$ 6,677	100.0%	44 %		
Gross profit	1,533	31.4	906	27.3	69	2,868	29.9	1,861	27.9	54		
Total operating expenses	988	20.2	655	19.7	51	2,091	21.8	1,288	19.3	62		
Operating income	545	11.1	251	7.6	117	777	8.1	573	8.6	36		
Net income (loss)	235	4.8	251	7.6	(6)	(131)	(1.4)	534	8.0	(125)		

The following table sets forth, for the periods presented, summary information regarding unit shipments, average selling prices (“ASPs”) and net revenues by geography and end market:

	Three Months Ended				Six Months Ended			
	December 30, 2016		January 1, 2016		December 30, 2016		January 1, 2016	
<i>(in millions, except exabytes, percentages and ASPs)</i>								
Revenue, net	\$ 4,888	\$ 3,317	\$ 9,602	\$ 6,677				
HDD ASPs (per unit)	\$ 62	\$ 61	\$ 61	\$ 61				
Revenues by Geography (%)								
Americas	39%	31%	39%	31%				
Europe, Middle East and Africa	17	23	17	22				
Asia	44	46	44	47				
Revenues by End Market (%)								
Client Devices	49%	48%	50%	49%				
Client Solutions	22	14	21	13				
Data Center Devices & Solutions	29	38	29	38				
HDD Unit Shipments								
	44	49	92	101				
Exabytes Shipped								
	78	69	158	133				

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Net Revenue

Net revenue for the three months ended December 30, 2016 increased \$1.6 billion , or 47% , compared to the same period in 2016 , which reflects an increase from NAND-flash products from our acquisition of SanDisk, partially offset by lower HDD unit shipments. Total HDD shipments for the three months ended December 30, 2016 decreased to 44 million units, as compared to 49 million units in the same period in 2016 , primarily due to lower HDD shipments for personal computer (“PC”) and performance enterprise. This was partially offset by an increase in HDD ASP per unit of \$1 compared to the same period in 2016 , primarily due to a change in product mix.

Net revenue for the six months ended December 30, 2016 increased \$2.9 billion , or 44% , compared to the same period in 2016 , which reflects an increase from NAND-flash products from our acquisition of SanDisk, partially offset by lower HDD unit shipments. Total HDD shipments for the six months ended December 30, 2016 decreased to 92 million units, as compared to 101 million units in the same period in 2016 , primarily due to lower HDD shipments.

For the three and six months ended December 30, 2016 and January 1, 2016 , no customer accounted for 10% or more of our net revenue. For the three and six months ended December 30, 2016 , our top 10 customers accounted for 43% and 42% , respectively. For each of the three and six months ended January 1, 2016 , our top 10 customers accounted for 44% of our net revenue.

Consistent with standard industry practice, we have sales incentive and marketing programs that provide customers with price protection and other incentives or reimbursements that are recorded as a reduction to gross revenue. For each of the three and six months ended December 30, 2016 , these programs represented 8% of gross revenues. For the three and six months ended January 1, 2016 , these programs represented 13% and 12% of gross revenues, respectively. These amounts generally vary according to several factors including industry conditions, seasonal demand, competitor actions, channel mix and overall availability of products. Changes in future customer demand and market conditions may require us to adjust our incentive programs as a percentage of gross revenue.

Net Revenue by Geography

Changes in the mix of net revenue by geography for the three and six months ended December 30, 2016 , compared to the same period in 2016 , reflect the additional revenues from our acquisition of SanDisk which has comparatively higher revenue in the Americas than our pre-acquisition business.

Net Revenue by End Market

Changes in the mix of net revenue by end market for the three and six months ended December 30, 2016 , compared to the same period in 2016 , also reflect the increase in revenues from our acquisition of SanDisk which has comparatively higher revenue in Client Devices and Data Center Devices and Solutions than our pre-acquisition business.

Gross Profit and Gross Margin

Gross profit for the three months ended December 30, 2016 was \$1.5 billion , an increase of \$627 million compared to the same period in 2016 , driven by gross profit from NAND-flash products from our acquisition of SanDisk. Gross profit as a percentage of net revenue was 31.4% in the three months ended December 30, 2016 , as compared to 27.3% in the same period in 2016 . The increase in gross profit was due primarily to higher margins on NAND-flash memory products, increased HDD ASPs and cost improvements resulting from integration activities. Gross profit in the three months ended December 30, 2016 was negatively impacted by amortization expense on acquired intangible assets, stock-based compensation, charges related to the implementation of cost-saving initiatives and acquisition related charges, which aggregated \$259 million , or 5.3% of revenue. Gross profit in the three months ended January 1, 2016 was negatively impacted by charges related to the implementation of cost-saving initiatives, amortization expense on acquired intangible assets and stock-based compensation, which aggregated \$39 million , or 1.2% of revenue.

Gross profit for the six months ended December 30, 2016 was \$2.9 billion , an increase of \$1.0 billion compared to the same period in 2016 , driven by the increased revenues from NAND-flash products from our acquisition of SanDisk. Gross profit as a percentage of net revenue was 29.9% in the six months ended December 30, 2016 , as compared to 27.9% in the same period in 2016 . The increase in gross profit was due primarily to higher margins on NAND-flash memory products and cost improvements resulting from integration activities. Gross profit in the six months ended December 30, 2016 was negatively impacted by amortization expense on acquired intangible assets, charges related to the implementation of cost-saving initiatives, stock-based compensation and acquisition related charges, which aggregated \$523 million , or 5.4% of revenue. Gross profit in the six months ended January 1, 2016 was negatively impacted by amortization expense on acquired intangible assets, charges related to the implementation of cost-saving initiatives and stock-based compensation, which aggregated was \$61 million , or 0.9% of revenue.

Operating Expenses

	Three Months Ended					Six Months Ended				
	December 30, 2016		January 1, 2016		% Change	December 30, 2016		January 1, 2016		% Change
	Amount	% of Rev	Amount	% of Rev		Amount	% of Rev	Amount	% of Rev	
<i>(in millions, except percentages)</i>										
Research and development	\$ 585	12.0%	\$ 389	11.7%	50%	\$ 1,224	12.7%	\$ 774	11.6%	58%
Selling, general and administrative	358	7.3	239	7.2	50	754	7.9	431	6.5	75
Employee termination, asset impairment and other charges	45	0.9	27	0.8	67	113	1.2	83	1.2	36
Total operating expenses	<u>\$ 988</u>	20.2	<u>\$ 655</u>	19.7	51	<u>\$ 2,091</u>	21.8	<u>\$ 1,288</u>	19.3	62

The increase in research and development (“R&D”) expense in the three and six months ended December 30, 2016 , compared to the same period in 2016 , was primarily related to our acquisition of SanDisk and continued development of NAND technology to complement our existing product offerings. The three and six months ended December 30, 2016 also included aggregate charges of \$49 million and \$102 million , respectively, related to share-based compensation expenses, charges related to the implementation of cost-saving initiatives and acquisition-related charges. These costs were partially offset by cost savings from our integration activities. The three and six months ended January 1, 2016 also included aggregate charges of \$20 million and \$36 million , respectively, related to share-based compensation expenses, charges related to the implementation of cost-saving initiatives and other charges.

The increase in selling, general and administrative (“SG&A”) expense in the three and six months ended December 30, 2016 , compared to the same period in 2016 , was primarily related to our acquisition of SanDisk. The three and six months ended December 30, 2016 also included aggregate charges of \$97 million and \$216 million , respectively, related to share-based compensation expenses, amortization expense on acquired intangible assets, charges related to the implementation of cost-saving initiatives and acquisition-related charges. The three and six months ended January 1, 2016 also included aggregate charges of \$90 million and \$120 million , respectively, related to share-based compensation expenses, acquisition-related charges, charges related to an arbitration award, amortization expense on acquired intangible assets, charges related to the implementation of cost-saving initiatives and other charges.

Employee termination and other charges were \$45 million and \$113 million in the three and six months ended December 30, 2016 , respectively, an increase of \$18 million and \$30 million from the three and six months ended January 1, 2016 , respectively. For additional information regarding employee termination, asset impairment and other charges, see Part I, Item 1, Note 13 of the Notes to Condensed Consolidated Financial Statements included in this Quarterly Report on Form 10-Q .

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Interest and Other Income (Expense)

	Three Months Ended					Six Months Ended				
	December 30, 2016		January 1, 2016		% Change	December 30, 2016		January 1, 2016		% Change
	Amount	% of Rev	Amount	% of Rev		Amount	% of Rev	Amount	% of Rev	
<i>(in millions, except percentages)</i>										
Interest income	\$ 5	0.1 %	\$ 5	0.2 %	100%	\$ 10	0.1 %	\$ 9	0.1 %	11%
Interest expense	(205)	(4.2)	(13)	(0.4)	**	(441)	(4.6)	(26)	(0.4)	**
Other income (expense), net	(24)	(0.5)	1	—	**	(296)	(3.1)	2	—	**
Total interest and other expense, net	\$ (224)	(4.6)	\$ (7)	(0.2)	**	\$ (727)	(7.6)	\$ (15)	(0.2)	**

** Amount not meaningful.

Interest expense increased for the three and six months ended December 30, 2016, compared to the same period in 2016, primarily due to the additional debt issued in connection with the acquisition of SanDisk.

Other income (expense), net for the three months ended December 30, 2016 was primarily comprised of foreign exchange losses. Other income (expense), net for the six months ended December 30, 2016 was primarily comprised of the write-off of debt issuance costs on the settlement of the original U.S. Term Loan B and Euro Term Loan B, loss on the settlement of our convertible debt instruments, and foreign exchange losses.

Income Tax Expense (Benefit)

	Three Months Ended					Six Months Ended				
	December 30, 2016		January 1, 2016		% Change	December 30, 2016		January 1, 2016		% Change
	Amount	% of Rev	Amount	% of Rev		Amount	% of Rev	Amount	% of Rev	
<i>(in millions, except percentages)</i>										
Income tax expense (benefit)	\$ 86	1.8%	\$ (7)	(0.2)%	**	\$ 181	1.9%	\$ 24	0.4%	**
Effective tax rate	27%		(3)%			362%		4%		

** Amount not meaningful.

Income tax expense of \$181 million for the six months ended December 30, 2016 is attributable primarily to discrete effects consisting of income tax expense from the integration of SanDisk of \$90 million and a valuation allowance on acquired tax attributes of \$109 million. Income tax expense related to the SanDisk integration is partially offset by income tax benefit from deductible debt issuance costs, debt discounts and prepayment fees from the debt refinancing of \$96 million. These discrete items are the primary drivers of the effective tax rate for the six months ended December 30, 2016.

The primary drivers for the difference between the effective tax rate for the three and six months ended December 30, 2016 and the U.S. Federal statutory rate of 35% are the current year generation of tax credits, tax holidays in Malaysia, the Philippines, Singapore and Thailand that expire at various dates from 2016 through 2029, for both periods, and the discrete items described above for the six months ended December 30, 2016. For the three and six months ended January 1, 2016, the difference between the effective tax rate and the U.S. Federal statutory rate of 35% is primarily due to tax holidays in Malaysia, the Philippines, Singapore and Thailand that expire at various dates from 2016 through 2029.

For additional information regarding income tax expense (benefit), see Part I, Item 1, Note 10 of the Notes to Condensed Consolidated Financial Statements included in this Quarterly Report on Form 10-Q.

Liquidity and Capital Resources

The following table summarizes our statements of cash flows for the six months ended December 30, 2016 and January 1, 2016 :

	Six Months Ended	
	December 30, 2016	January 1, 2016
	<i>(in millions)</i>	
Net cash flow provided by (used in):		
Operating activities	\$ 1,500	\$ 1,143
Investing activities	(316)	(454)
Financing activities	(4,386)	(350)
Effect of exchange rate changes on cash	(9)	—
Net increase (decrease) in cash and cash equivalents	<u>\$ (3,211)</u>	<u>\$ 339</u>

We believe our current cash, cash equivalents and cash generated from operations as well as our available credit facilities will be sufficient to meet our working capital, debt, dividend and capital expenditure needs for at least the next twelve months. Our ability to sustain our working capital position is subject to a number of risks that we discuss in Part II, Item 1A in this Quarterly Report on Form 10-Q .

The cash on hand and indebtedness used to finance our acquisition of SanDisk could cause us to place more reliance on cash generated from operations to pay principal and interest on our debt, thereby reducing the availability of our cash flow for working capital, capital expenditure needs, dividends, or to pursue other potential strategic plans.

During 2017, we expect cash used for purchases of property, plant and equipment, and net activity in notes receivable and equity investments relating to our business ventures with Toshiba Corporation (“Flash Ventures”) to be approximately \$0.7 billion to \$1.1 billion of our cash. The total expected cash to be used could vary depending on the timing and completion of various capital projects and the availability, timing and terms of related financing.

A total of \$3.9 billion and \$6.9 billion of our cash and cash equivalents was held outside of the U.S. as of December 30, 2016 and July 1, 2016 , respectively. Our current plans anticipate we can meet our U.S. cash needs while continuing to permanently reinvest the undistributed earnings of our foreign subsidiaries. In the event the reinvested earnings of our foreign subsidiaries are distributed to the U.S., such a distribution could result in the accrual and payment of additional taxes.

Operating Activities

Cash flow from operating activities consists of net income, adjusted for non-cash charges, plus or minus working capital changes. This represents our principal source of cash. Net cash provided by changes in working capital was \$37 million for the six months ended December 30, 2016 , as compared to \$1 million for the six months ended January 1, 2016 .

Our working capital requirements primarily depend on the effective management of our cash conversion cycle, which measures how quickly we can convert our products into cash through sales. The cash conversion cycles for the six months ended December 30, 2016 and January 1, 2016 were as follows:

	Six Months Ended	
	December 30, 2016	January 1, 2016
	<i>(in days)</i>	
Days sales outstanding	38	47
Days in inventory	56	48
Days payables outstanding	(59)	(71)
Cash conversion cycle	<u>35</u>	<u>24</u>

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For the six months ended December 30, 2016, our days sales outstanding (“DSOs”) decreased by 9 days, days in inventory (“DIOs”) increased by 8 days and days payables outstanding (“DPOs”) decreased by 12 days, as compared to the prior year. Changes in DSOs are generally due to the linearity of shipments. Changes in DIOs are generally related to the timing of inventory builds. Changes in DPOs are generally related to production volume and the timing of purchases during the period. From time to time, we modify the timing of payments to our vendors. We make modifications primarily to manage our vendor relationships and to manage our cash flows, including our cash balances. Generally, we make the payment term modifications through negotiations with our vendors or by granting to, or receiving from, our vendors’ payment term accommodations.

Investing Activities

Net cash used in investing activities in the six months ended December 30, 2016 was \$316 million, as compared to \$454 million net cash used in investing activities in the six months ended January 1, 2016. During the six months ended December 30, 2016, net cash used in investing activities primarily consisted of \$330 million of capital expenditures and a net \$70 million increase in notes receivable to and investments in Flash Ventures, partially offset by a net \$95 million decrease in our investments in marketable securities. During the six months ended January 1, 2016, net cash used in investing activities primarily consisted of \$300 million of capital expenditures and a net \$142 million increase in investments in marketable securities.

Our cash equivalents are primarily invested in highly liquid money market funds that are invested in U.S. Treasury securities and U.S. Government Agency securities. In addition, we invest directly in U.S. Treasury securities, U.S. and International Government Agency securities, certificates of deposit, asset-backed securities, and corporate and municipal notes and bonds.

Financing Activities

Net cash used in financing activities was \$4.4 billion in the six months ended December 30, 2016, as compared to net cash used in financing activities of \$350 million in the six months ended January 1, 2016. During the six months ended December 30, 2016, net cash used in financing activities consisted of \$8.3 billion to repay debt and \$284 million to pay dividends on our common stock, partially offset by \$4.0 billion of proceeds from debt, net of issuance costs, \$61 million of proceeds from call options and a net \$106 million provided by employee stock plans. During the six months ended January 1, 2016, net cash used in financing activities primarily consisted of \$231 million to pay dividends on our common stock, \$60 million to repurchase shares of our common stock and \$63 million to repay debt.

Off-Balance Sheet Arrangements

Other than the commitments related to Flash Ventures, facility lease commitments incurred in the normal course of business and certain indemnification provisions (see “Contractual Obligations and Commitments” below), we do not have any other material off-balance sheet financing arrangements or liabilities, guarantee contracts, retained or contingent interests in transferred assets, or any other obligation arising out of a material variable interest in an unconsolidated entity. We do not have any majority-owned subsidiaries that are not included in the condensed consolidated financial statements. Additionally, we do not have an interest in, or relationships with, any special-purpose entities. For additional information regarding our off-balance sheet arrangements, see Part I, Item 1, Note 8 of the Notes to Condensed Consolidated Financial Statements included in this Quarterly Report on Form 10-Q.

Short and Long-term Liquidity

Contractual Obligations and Commitments

The following is a summary of our known contractual cash obligations and commercial commitments as of December 30, 2016 :

	Total	1 Year (Remaining 6 months of 2017)	2-3 Years (2018- 2019)	4-5 Years (2020- 2021)	More than 5 Years (Beyond 2021)
	<i>(in millions)</i>				
Long-term debt, including current portion	\$ 13,299	\$ 20	\$ 595	\$ 3,724	\$ 8,960
Interest on debt	5,288	393	1,646	1,646	1,603
Flash Ventures and other related commitments ⁽¹⁾	6,336	769	3,412	1,479	676
Operating leases	181	33	78	47	23
Purchase obligations	700	693	7	—	—
Total	\$ 25,804	\$ 1,908	\$ 5,738	\$ 6,896	\$ 11,262

⁽¹⁾ Includes reimbursement for depreciation and lease payments on owned and committed equipment, funding commitments for loans and equity investments and reimbursement for other committed expenses, including R&D. Funding commitments assume no additional operating lease guarantees. Additional operating lease guarantees can reduce funding commitments.

Debt

The Credit Agreement (as defined in Part I, Item 1, Note 6 of the Notes to Condensed Consolidated Financial Statements included in this Quarterly Report on Form 10-Q) requires us to comply with certain financial covenants, such as a leverage ratio and an interest coverage ratio. In addition, the documents governing substantially all of our outstanding debt, including the Credit Agreement, require us to comply with customary covenants that limit or restrict us and our subsidiaries' ability to incur liens and indebtedness; make certain restricted payments, acquisitions, investments, loans and guarantees; and enter into certain transactions with affiliates, mergers and consolidations. As of December 30, 2016, we were in compliance with these covenants.

See Part I, Item 1, Note 6 of the Notes to Condensed Consolidated Financial Statements included in this Quarterly Report on Form 10-Q for information regarding our indebtedness.

Flash Ventures

Flash Ventures sells and leases back from a consortium of financial institutions a portion of its tools and has entered into equipment lease agreements of which we guarantee half of the total outstanding obligations. The lease agreements contain customary covenants for Japanese lease facilities. In addition to containing customary events of default related to Flash Ventures that could result in an acceleration of Flash Ventures' obligations, the lease agreements contain acceleration clauses for certain events of default related to the guarantors, including us. As of December 30, 2016, we were in compliance with all covenants under these Japanese lease facilities.

See Part I, Item 1, Note 8 of the Notes to Condensed Consolidated Financial Statements included in this Quarterly Report on Form 10-Q for information regarding Flash Ventures.

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Foreign Exchange Contracts

We purchase foreign exchange contracts to hedge the impact of foreign currency fluctuations on certain underlying assets, liabilities and commitments for operating expenses and product costs denominated in foreign currencies. For a description of our current foreign exchange contract commitments, see Part I, Item 3, under the heading “ Disclosure About Foreign Currency Risk ,” and Part I, Item 1, Note 5 of the Notes to Condensed Consolidated Financial Statements included in this Quarterly Report on Form 10-Q .

Indemnifications

In the ordinary course of business, we may provide indemnifications of varying scope and terms to customers, vendors, lessors, business partners and other parties with respect to certain matters, including, but not limited to, losses arising out of our breach of agreements, products or services to be provided by us, environmental compliance or from intellectual property infringement claims made by third parties. In addition, we have entered into indemnification agreements with our directors and certain of our officers that will require us, among other things, to indemnify them against certain liabilities that may arise by reason of their status or service as directors or officers. We maintain director and officer insurance, which may cover certain liabilities arising from our obligation to indemnify our directors and officers in certain circumstances.

It is not possible to determine the maximum potential amount under these indemnification agreements due to the limited history of prior indemnification claims and the unique facts and circumstances involved in each particular agreement. Such indemnification agreements may not be subject to maximum loss clauses. Historically, we have not incurred material costs as a result of obligations under these agreements.

Unrecognized Tax Benefits

As of December 30, 2016 , the amount of unrecognized tax benefits, including related accrued interest and penalties, was \$561 million , of which \$445 million could result in potential cash payments. We are not able to provide a reasonable estimate of the timing of future tax payments related to these obligations. For additional information regarding our total tax liability for unrecognized tax benefits, see Part I, Item 1, Note 10 of the Notes to Condensed Consolidated Financial Statements included in this Quarterly Report on Form 10-Q .

Cash Dividend

Since the first quarter of 2014, we have issued a quarterly cash dividend. On November 3, 2016 , we declared a cash dividend of \$0.50 per share of our common stock to our shareholders of record as of December 30, 2016 . The cash dividend of \$144 million was paid on January 17, 2017 . On February 1, 2017 , we declared a cash dividend of \$0.50 per share of our common stock to our shareholders of record as of March 31, 2017 . The cash dividend will be paid on April 17, 2017 . We may modify, suspend, or cancel our cash dividend policy in any manner and at any time.

Critical Accounting Policies and Estimates

We have prepared the accompanying unaudited condensed consolidated financial statements in accordance with accounting principles generally accepted in the United States. The preparation of the financial statements requires the use of judgments and estimates that affect the reported amounts of revenues, expenses, assets, liabilities and shareholders' equity. We have adopted accounting policies and practices that are generally accepted in the industry in which we operate. If these estimates differ significantly from actual results, the impact to the condensed consolidated financial statements may be material.

There have been no material changes in our critical accounting policies and estimates from those disclosed in our Annual Report on Form 10-K for our fiscal year ended July 1, 2016 . Please refer to Part II, Item 7 of our Annual Report on Form 10-K for the fiscal year ended July 1, 2016 for a discussion of our critical accounting policies and estimates.

Recent Accounting Pronouncements

In October 2016, the FASB issued ASU No. 2016-16, “Income Taxes (Topic 740): Intra-Entity Transfers of Assets Other Than Inventory” (“ASU 2016-16”). The new standard removes the prohibition in the FASB Accounting Standards Codification (“ASC”) Topic 740 against the immediate recognition of the current and deferred income tax effects of intra-entity transfers of assets other than inventory. The ASU is intended to reduce the complexity of U.S. GAAP and diversity in practice related to the tax consequences of certain types of intra-entity asset transfers, particularly those involving intellectual property. The new standard is effective for fiscal years beginning after December 15, 2017, which for us is the first quarter of 2019. Early adoption is permitted. We are currently evaluating the impact ASU 2016-16 will have on our consolidated financial statements.

In August 2016, the FASB issued ASU No. 2016-15, “Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments” (“ASU 2016-15”). The new standard addresses certain cash flows issues regarding the classification of certain cash receipts and cash payments, which, among others, includes our disclosure requirement related to debt prepayment or extinguishment costs and distributions received from equity method investees. The new standard is effective for fiscal years beginning after December 15, 2017, which for us is the first quarter of 2019. Early adoption is permitted. We expect to adopt this standard in the first quarter of 2018. The adoption of this standard is not expected to have a material impact on our consolidated financial statements.

In March 2016, the FASB issued ASU No. 2016-09, “Compensation — Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting” (“ASU 2016-09”). The new standard simplifies several aspects of the accounting for share-based payment transactions and states that, among other things, all excess tax benefits and tax deficiencies should be recognized as income tax expense or benefit in the income statement and an entity can make an entity-wide accounting policy election to either estimate the number of awards that are expected to vest or account for forfeitures when they occur. The new standard is effective for fiscal years beginning after December 15, 2016, and interim periods within those years, which for us is the first quarter of 2018. Early adoption is permitted. We expect to adopt this standard in the first quarter of 2018. We are currently evaluating the impact ASU 2016-09 will have on our consolidated financial statements and related disclosures.

In February 2016, the FASB issued ASU No. 2016-02, “Leases (Topic 842)” (“ASU 2016-02”). The new standard, among other things, requires lessees to recognize a right-of-use asset and a lease liability for leases. The new standard is effective for fiscal years beginning after December 15, 2018, which for us is the first quarter of 2020. Early adoption is permitted. We expect to adopt this standard in the first quarter of 2020. We are currently evaluating the impact ASU 2016-02 will have on our consolidated financial statements and related disclosures.

In January 2016, the FASB issued ASU No. 2016-01, “Financial Instruments — Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities” (“ASU 2016-01”), which provides guidance related to accounting for equity investments, financial liabilities under the fair value option, and the presentation and disclosure requirements for financial instruments. In addition, the FASB clarified guidance related to the valuation allowance assessment when recognizing deferred tax assets resulting from unrealized losses on available-for-sale debt securities. ASU 2016-01 is effective for fiscal years beginning after December 15, 2017, which for us is the first quarter of 2019. Early adoption is not permitted. We are currently evaluating the impact ASU 2016-01 will have on our consolidated financial statements.

In May 2014, the FASB issued ASU No. 2014-09, “Revenue from Contracts with Customers (Topic 606)”, which amends the guidance in former ASC Topic 605, “Revenue Recognition”, to provide a single, comprehensive revenue recognition model for all contracts with customers. ASC Topic 606 requires an entity to recognize revenue in a manner that depicts the transfer of promised goods or services to customers in amounts that reflect the consideration to which an entity expects to be entitled in exchange for those goods or services. The new standard also requires entities to enhance disclosures about the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers. As currently issued and amended, the standard is effective for public business entities applying U.S. GAAP, for annual periods commencing or after December 16, 2017 (with early adoption permitted for annual periods beginning on or after December 16, 2016). We intend to apply the new standard starting from the first quarter of fiscal 2019. The standard may be applied retrospectively to all prior periods presented (“full retrospective method”), or retrospectively with the cumulative effect of initially applying the guidance recognized at the date of initial application (“modified retrospective method”). Based on our preliminary plan, we intend to adopt the new standard using the modified retrospective method. However, we continue to assess this in connection with our entire project plan.

We expect the implementation of the new standard to impact the recognition of our revenue as follows:

- Substantially all of our current revenue is from the sale of hardware products. We do not expect any material changes to the timing or amount of revenue for these types of sales under the new standard.
- For sales-based royalties, we will need to estimate and recognize revenue in the period the royalty-bearing sales occur as opposed to the existing treatment of recognizing revenue in the period the royalty report is received. This change will result in the acceleration of revenue recognition by one fiscal quarter as well as fluctuations between the estimated and actual reported sales-based royalties.
- For software and intellectual property licenses, we are still assessing the impact and timing to revenue from the implementation of the new standard. However, we do not currently expect the new standard to have a material impact on our revenue for these types of arrangements.
- Our revenue disclosures are expected to expand.

We are still assessing the impact to our processes and systems configuration from the implementation of the new revenue standard and do not currently expect any significant changes to our other accounting policies from the adoption of the new revenue standard. Our implementation efforts are progressing as planned.

For a description of recently adopted accounting pronouncements, including the respective dates of adoption and effects on our results of operations and financial condition, see Part I, Item 1, Note 2 of the Notes to Condensed Consolidated Financial Statements included in this Quarterly Report on Form 10-Q, which is incorporated by reference in response to this item.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Disclosure About Foreign Currency Risk

Although the majority of our transactions are in U.S. dollars, some transactions are based in various foreign currencies. We purchase short-term, foreign exchange contracts to hedge the impact of foreign currency exchange fluctuations on certain underlying assets, liabilities and commitments for operating expenses and product costs denominated in foreign currencies. The purpose of entering into these hedge transactions is to minimize the impact of foreign currency fluctuations on our results of operations. The contract maturity dates do not exceed 12 months. We do not purchase foreign exchange contracts for speculative or trading purposes. For additional information, see Part I, Item 1, Notes 4 and 5 of the Notes to Condensed Consolidated Financial Statements included in this Quarterly Report on Form 10-Q.

As of December 30, 2016, we had outstanding the foreign exchange contracts presented in the following table. The changes in fair values of these foreign exchange contracts would be largely offset in other income (expense) by corresponding changes in the fair values of the foreign currency denominated monetary assets and liabilities.

	Contract Amount	Weighted Average Contract Rate ⁽¹⁾	Unrealized Gain (Loss)
	<i>(in millions, except weighted average contract rate)</i>		
Foreign exchange contracts:			
Cash flow hedges:			
Japanese yen	\$ 919	108.59	\$ (58)
Malaysian ringgit	128	4.24	(6)
Philippine peso	43	48.61	(1)
Singapore dollar	36	1.40	(1)
Thailand baht	370	35.11	(7)
Fair value hedges:			
British pound sterling	\$ 15	0.81	\$ —
Euro	38	0.94	—
Japanese yen	208	102.30	—
Malaysian ringgit	14	4.49	—
Philippine peso	22	50.28	—
Singapore dollar	11	1.43	—
Thailand baht	143	35.60	—

⁽¹⁾ Expressed in units of foreign currency per U.S. dollar.

During the three and six months ended December 30, 2016 and January 1, 2016, total net realized transaction and foreign exchange contract currency gains and losses were not material to our condensed consolidated financial statements.

Notwithstanding our efforts to mitigate some foreign exchange risks, we do not hedge all of our foreign currency exposures, and there can be no assurance that our mitigating activities related to the exposures that we hedge will adequately protect us against risks associated with foreign currency fluctuations.

Disclosure About Other Market Risks

Variable Interest Rate Risk

Borrowings under our Term Loan A and our revolving credit facility bear interest at a rate per annum, at our option, of either an adjusted LIBOR rate (subject to a 0.0% floor) plus an applicable margin of 2.0% or at a base rate plus an applicable margin of 1.0% . The applicable margin for the borrowings under our Term Loan A and our revolving credit facility will range, depending on our leverage, from 1.50% to 2.25% for LIBOR loans and from 0.50% to 1.25% for base rate loans.

Borrowings under the U.S. Term Loan B-1 tranche bear interest at a rate per annum, at our option, of an adjusted LIBOR rate, subject to a 0.75% floor, plus 3.75% or a base rate plus 2.75% (4.52% as of December 30, 2016). Borrowings under the Euro Term Loan B-1 tranche bear interest at a rate per annum, at our option, equal to an adjusted EURIBOR rate, subject to a 0.75% floor, plus 3.25% (4.00% as of December 30, 2016).

As of December 30, 2016 , we had \$8.0 billion of long-term variable rate debt outstanding, and a one percent increase in the variable rate of interest, subject to each loan specific floor, would have increased annual interest expense by \$71 million .

For additional information regarding our term loans, see Part I, Item 1, Note 6 of the Notes to Condensed Consolidated Financial Statements included in this Quarterly Report on Form 10-Q and Part II, Item 8, Note 3 of the Notes to Consolidated Financial Statements included in our Annual Report on Form 10-K for the fiscal year ended July 1, 2016.

Item 4. Controls and Procedures

As required by Rule 13a-15(b) promulgated by the Securities and Exchange Commission (“SEC”) under the Securities Exchange Act of 1934, as amended (the “Exchange Act”), we carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures (as such term is defined in Rule 13a-15(e) under the Exchange Act) as of the end of the period covered by this Quarterly Report on Form 10-Q. Based on that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that, as of the end of the period covered by this Quarterly Report on Form 10-Q, our disclosure controls and procedures were effective.

There has been no change in our internal control over financial reporting during the second quarter ended December 30, 2016 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. *Legal Proceedings*

For a description of our legal proceedings, see Part I, Item 1, Note 14 of the Notes to Condensed Consolidated Financial Statements included in this Quarterly Report on Form 10-Q, which is incorporated by reference in response to this item.

Item 1A. *Risk Factors*

The business, financial condition and operating results of the Company can be affected by a number of risks and uncertainties, whether currently known or unknown, any one or more of which could, directly or indirectly, cause the Company's actual results of operations and financial condition to vary materially from past, or from anticipated future, results of operations and financial condition. The risks and uncertainties discussed below are not the only ones facing our business, but do represent those risks and uncertainties that we believe are material to us. Additional risks and uncertainties not presently known to us or that we currently deem immaterial may also adversely affect our business, financial condition, results of operations or the market price of our common stock.

Adverse global economic conditions and credit market uncertainty could harm our business, results of operations and financial condition.

Adverse global economic conditions and uncertain conditions in the credit market have had, and in the future could have, a significant adverse effect on our company and on the storage industry as a whole. Several factors contribute to these conditions and this uncertainty, including, but not limited to, volatility in the equity, credit and other financial markets and real estate markets, slower growth in certain geographic regions, lower levels of consumer liquidity, risk of default on sovereign debt, higher interest rates, materials and component cost increases, political uncertainty and other macroeconomic factors, such as the June 2016 referendum by British voters to exit the European Union, commonly referred to as "Brexit," and changes to policies, rules and regulations which may be proposed or implemented by the new U.S. President and his administration. Some of the risks and uncertainties we face as a result of these conditions include the following:

- **Volatile Demand and Supplier Risk.** Our direct and indirect customers may delay or reduce their purchases of our products and systems containing our products. In addition, many of our customers rely on credit financing to purchase our products. If negative conditions in the global credit markets prevent our customers' access to credit, product orders may decrease, which could result in lower revenue. Likewise, if our suppliers, sub-suppliers and sub-contractors (collectively referred to as "suppliers"), or partners face challenges in obtaining credit, in selling their products or otherwise in operating their businesses, they may be unable to offer the materials we use to manufacture our products. These actions could result in reductions in our revenue and increased operating costs, which could adversely affect our business, results of operations and financial condition.
- **Restructuring Activities.** If demand for our products slows as a result of a deterioration in economic conditions, we may undertake restructuring activities to realign our cost structure with softening demand. The occurrence of restructuring activities could result in impairment charges and other expenses, which could adversely impact our results of operations and financial condition.
- **Credit Volatility and Loss of Receivables.** We extend credit and payment terms to some of our customers. In addition to ongoing credit evaluations of our customers' financial condition, we traditionally seek to mitigate our credit risk by purchasing credit insurance on certain of our accounts receivable balances. As a result of the continued uncertainty and volatility in global economic conditions; however, we may find it increasingly difficult to be able to insure these accounts receivable. We could suffer significant losses if a customer whose accounts receivable we have not insured, or have underinsured, fails to pay us on their accounts receivable balances. Additionally, negative or uncertain global economic conditions increase the risk that if a customer we have insured fails to pay us on their accounts receivable, the financial condition of the insurance carrier for such customer account may have also deteriorated such that it cannot cover our loss. A significant loss of accounts receivable that we cannot recover through credit insurance would have a negative impact on our financial condition.

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- Impairment Charges. We test goodwill for impairment annually as of the first day of our fourth quarter and at other times if events have occurred or circumstances exist that indicate the carrying value of goodwill may no longer be recoverable. Negative or uncertain global economic conditions could result in circumstances, such as a sustained decline in our stock price and market capitalization or a decrease in our forecasted cash flows, indicating that the carrying value of our long-lived assets or goodwill may be impaired. If we are required to record a significant charge to earnings in our consolidated financial statements because of an impairment of our long-lived assets or goodwill, our results of operations will be adversely affected.

Integrating SanDisk Corporation's ("SanDisk") operations with ours may be more difficult, costly or time consuming than expected and the anticipated benefits, synergies and cost savings of our recent acquisition of SanDisk (the "Merger") may not be realized.

The success of our recent acquisition of SanDisk, including anticipated benefits, synergies and cost savings, will depend, in part, on our ability to successfully combine and integrate the businesses and culture of SanDisk into our company. It is possible that the integration process will take longer than anticipated. In addition, the integration process could result in the loss of key employees, higher than expected costs, ongoing diversion of management attention, the disruption of our ongoing businesses or inconsistencies in standards, controls, procedures and policies that adversely affect our ability to maintain relationships with customers, vendors, partners and employees. If we experience difficulties with the integration process, the anticipated benefits of the Merger may not be realized fully or at all, or may take longer to realize than expected. In addition, the actual cost savings of the Merger could be less than anticipated. Additionally, the integration of SanDisk's operations into our operations may also increase the risk that our internal controls are found to be ineffective.

Achieving the benefits of the Merger will depend, in part, on our ability to integrate the business and operations of SanDisk successfully and efficiently with our business. The challenges involved in this integration, which will be complex and time-consuming, include, but are not limited to, the following:

- difficulties entering new markets or manufacturing in new geographies where we have no or limited direct prior experience;
- successfully managing relationships with our strategic partners, and our combined supplier and customer base;
- coordinating and integrating independent research and development ("R&D") and engineering teams across technologies and product platforms to enhance product development while reducing costs;
- increased levels of investment in R&D, manufacturing capability and technology enhancement relating to SanDisk's business;
- successfully transitioning to 3-dimensional ("3D") NAND and future technologies;
- coordinating sales and marketing efforts to effectively position the combined company's capabilities and the direction of product development;
- difficulties in integrating the systems and processes of two companies with complex operations and multiple manufacturing sites;
- the increased scale and complexity of our operations resulting from the Merger;
- retaining key employees;
- obligations that we will have to counterparties of SanDisk that arise as a result of the change in control of SanDisk; and
- the diversion of management attention from other important business objectives.

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If we do not successfully manage these issues and the other challenges inherent in integrating an acquired business of the size and complexity of SanDisk, then we may not achieve the anticipated benefits of the Merger and our revenue, expenses, operating results and financial condition could be materially adversely affected.

Our high level of debt may have an adverse impact on our liquidity, restrict our current and future operations, particularly our ability to respond to business opportunities, and increase our vulnerability to adverse economic and industry conditions.

In connection with the Merger, we substantially increased our indebtedness, which could adversely affect our ability to fulfill our obligations and have a negative impact on our financing options and liquidity position. As of December 30, 2016, our total indebtedness was \$13.3 billion, and we had \$1.0 billion of additional borrowing availability under our revolving credit facility.

Our high level of debt could have significant consequences, which include, but are not limited to, the following:

- limiting our ability to obtain additional financing in the future for working capital, capital expenditures, acquisitions or other general corporate purposes;
- requiring a substantial portion of our cash flows to be dedicated to debt service payments instead of other purposes, thereby reducing the amount of cash flows available for working capital, capital expenditures, acquisitions, R&D and other general corporate purposes;
- imposing financial and other restrictive covenants on our operations, including limiting our ability to (i) declare or pay dividends or purchase our common stock; (ii) purchase assets, make investments, complete acquisitions, consolidate or merge with or into, or sell all or substantially all of our assets to, another person; (iii) dispose of assets; (iv) incur liens; and (v) enter into transactions with affiliates;
- placing us at a competitive disadvantage to competitors carrying less debt; and
- making us more vulnerable to economic downturns and limiting our ability to withstand competitive pressures or take advantage of new opportunities to grow our business.

Our ability to meet the debt service obligations contained in our debt agreements will depend on our available cash and our future performance, which will be affected by financial, business, economic and other factors, including potential changes in laws or regulations, industry conditions, industry supply and demand balance, customer preferences, the success of our products and pressure from competitors. If we are unable to meet our debt service obligations or should we fail to comply with our financial and other restrictive covenants contained in the agreements governing our indebtedness, causing an event of default under the applicable indebtedness, the debt holders could accelerate the related debt and that may result in the acceleration of any other debt, leases or other obligations to which a cross acceleration or cross-default provision applies. If we are required to repay our indebtedness before their due dates, we may not have sufficient funds available to repay such indebtedness and we may be required to refinance all or part of our debt, sell important strategic assets at unfavorable prices, incur additional indebtedness or issue common stock or other equity securities. We may not be able to, at any given time, refinance our debt, sell assets, incur additional indebtedness or issue equity securities on terms acceptable to us, in amounts sufficient to meet our needs or at all. Our inability to service our debt obligations or refinance our debt could have a material adverse effect on our business, operating results and financial condition. Further, if we are unable to repay, refinance or restructure our secured indebtedness, the holder of such debt could proceed against the collateral securing that indebtedness. Refinancing our indebtedness may also require us to expense previous debt issuance costs or to incur new debt issuance costs.

In addition, our credit ratings impact the cost and availability of future borrowings and, accordingly, our cost of capital. Our ratings reflect the opinions of the ratings agencies of our financial strength, operating performance and ability to meet our debt obligations. There can be no assurance that we will achieve a particular rating or maintain a particular rating in the future.

We may from time to time seek to refinance the substantial indebtedness we incurred to finance the Merger by issuing additional shares of our common stock in one or more securities offerings. These securities offerings may dilute our existing shareholders, reduce the value of our common stock, or both. Because our decision to issue securities will depend on, among other things, market conditions and other factors beyond our control, we cannot predict or estimate the amount, timing or nature of any future securities offerings. Thus, holders of our common stock bear the risk of our future offerings diluting and potentially reducing the value of our common stock.

If we are unable to successfully integrate the business and operations of HGST, our business and financial condition may be adversely affected.

In connection with obtaining the regulatory approvals required to complete the acquisition of HGST, we agreed to certain conditions required by the Ministry of Commerce of the People's Republic of China ("MOFCOM"), including adopting measures to keep HGST as an independent competitor until MOFCOM agreed otherwise. On October 19, 2015, MOFCOM announced that it had made a decision allowing us to integrate substantial portions of our HGST and WD subsidiaries, provided that we continue to offer both HGST and WD product brands and maintain separate sales teams that will separately offer products under the WD and HGST brands for two years from the date of the decision.

As a result of MOFCOM's decision, we immediately began planning for the integration of the substantial portions of our HGST and WD subsidiaries that we are now allowed to integrate (including corporate functions, R&D, recording heads and magnetic media operations, engineering and manufacturing). We expect this integration to continue through the end of calendar year 2017. Our integration efforts during this time may involve significant management time and create uncertainty for employees and customers. Any delays in the integration process could have a material adverse effect on our business, results of operations and financial condition. It is possible that the integration process could result in the loss of key employees, the loss of customers, the disruption of our company's ongoing business or in unexpected integration issues, higher than expected integration costs and an overall integration process that takes longer than originally anticipated. Additionally, the integration of the operations of our HGST and Western Digital Technologies, Inc. ("WDT") subsidiaries may also increase the risk that our internal controls are found to be ineffective. Further, until we are able to begin combining our HGST and WD product brands and sales teams on October 19, 2017, we will continue to incur additional costs to maintain separate brands and sales teams. These additional costs, along with any delay in the integration process or higher than expected integration costs or other integration issues, could adversely affect our ability to achieve the full operating expense synergies we expect from integration of the businesses of our HGST and WDT subsidiaries. Any failure to achieve the full operating expense synergies that we expect from this integration could harm our business and financial condition. Achieving these synergies is also subject to significant business, operational, economic and competitive uncertainties and contingencies, and we cannot assure you that any or all of these synergies will be achieved in the anticipated amounts or within the anticipated time frames or cost expectations or at all.

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We participate in a highly competitive industry that is subject to declining average selling prices (“ASPs”), volatile gross margins and significant shifts in market share, all of which could adversely affect our operating results and financial condition.

Demand for our devices, software and solutions that we offer to our customers, which we refer to in this Item 1A as our “products”, depends in large part on the demand for systems (including personal computers (“PCs”) and mobile devices) manufactured by our customers and on storage upgrades to existing systems. The demand for systems has been volatile in the past and often has had an exaggerated effect on the demand for our products in any given period. The price of NAND flash memory is influenced by, among other factors, the balance between supply and demand, including the effects of new fab capacity in the industry, macroeconomic factors, business conditions, technology transitions, conversion of industry DRAM capacity to NAND, conversion of 2-dimensional (“2D”) NAND capacity to 3D NAND or other actions taken by us or our competitors. The price of hard disk drives (“HDDs”) is influenced by, among other factors, the balance between supply and demand, including the effects of new fab capacity in the industry, macroeconomic factors, business conditions, technology transitions, and other actions taken by us or our competitors. The storage market has experienced periods of excess capacity, which can lead to liquidation of excess inventories and significant reductions in price. If these price changes occur unnecessarily or in an unexpected manner, there will likely be an adverse impact on our revenue and gross margins. In addition, we compete based on our ability to offer our customers competitive solutions that provide the most current and desired product and service features. We expect that competition will continue to be intense, and there is a risk that our competitors’ products may be less costly, provide better performance or include additional features when compared to our products. Our ASPs and gross margins also tend to decline when there is a shift in the mix of product sales, and sales of lower priced products increase relative to those of higher priced products. Further, we face potential gross margin pressures resulting from our ASPs declining more rapidly than our cost of goods sold. Rapid technological changes often reduce the volume and profitability of sales of existing products and increase the risk of inventory obsolescence. These factors, along with others, may also result in significant shifts in market share among the industry’s major participants, including a substantial decrease in our market share, all of which could adversely impact our operating results and financial condition.

Our failure to accurately forecast market and customer demand for our products, or to quickly adjust to forecast changes, could adversely affect our business and financial results or operating efficiencies.

The data storage industry faces difficulties in accurately forecasting market and customer demand for its products. The variety and volume of products we manufacture are based in part on these forecasts. Accurately forecasting demand has become increasingly difficult for us, our customers and our suppliers in light of the volatility in global economic conditions and industry consolidation, resulting in less availability of historical market data for certain product segments. Further, for many of our original equipment manufacturers (“OEMs”) utilizing just-in-time inventory, we do not generally require firm order commitments and instead receive a periodic forecast of requirements, which may prove to be inaccurate. In addition, because our products are designed to be largely interchangeable with competitors’ products, our demand forecasts may be impacted significantly by the strategic actions of our competitors. As forecasting demand becomes more difficult, the risk that our forecasts are not in line with demand increases. If our forecasts exceed actual market demand, then we could experience periods of product oversupply, excess inventory and price decreases, which could impact our financial performance. If market demand increases significantly beyond our forecasts or beyond our ability to add manufacturing capacity, then we may not be able to satisfy customer product needs, possibly resulting in a loss of market share if our competitors are able to meet customer demands. In addition, some of our components have long lead-times, requiring us to place orders several months in advance of anticipated demand. Such long lead-times increase the risk of excess inventory or loss of sales in the event our forecasts vary substantially from actual demand.

We experience significant sales seasonality and cyclicalities, which could cause our operating results to fluctuate.

Sales of computer systems, mobile devices, storage subsystems, gaming consoles and consumer electronics (“CE”) tend to be seasonal and cyclical, and therefore we expect to continue to experience seasonality and cyclicalities in our business as we respond to variations in our customers’ demand for our products. However, changes in seasonal and cyclical patterns have made it, and could continue to make it, more difficult for us to forecast demand, especially as a result of the current macroeconomic environment. Changes in the product or channel mix of our business can also impact seasonal and cyclical patterns, adding complexity in forecasting demand. Seasonality and cyclicalities also may lead to higher volatility in our stock price. It is difficult for us to evaluate the degree to which seasonality and cyclicalities may affect our stock price or business in future periods because of the rate and unpredictability of product transitions and new product introductions and macroeconomic conditions.

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Our sales to the CE, cloud computing, network attached storage (“NAS”), surveillance systems and enterprise markets, which have accounted for and may continue accounting for an increasing percentage of our overall revenue, may grow at a slower rate than current estimates or not at all, which could materially adversely impact our operating results and financial condition.

The secular growth of digital data has resulted in a more diversified mix of revenue from the CE, cloud computing, NAS, surveillance systems and enterprise markets. As sales into these markets have become a more significant portion of our revenue, events or circumstances that adversely impact demand in these markets, or our inability to address that demand successfully, could materially adversely impact our operating results. For example, demand in, or our sales to, these markets may be adversely affected by the following:

- **Mobile Devices.** There has been and continues to be a rapid growth in devices that do not contain a hard drive such as tablet computers and smart phones. As tablet computers and smart phones provide many of the same capabilities as PCs, they have displaced or materially affected, and we expect will continue to displace or materially affect, the demand for PCs. If we are not successful in adapting our product offerings to include disk drives or alternative storage solutions that address these devices, even after our acquisition of SanDisk, demand for our products in these markets may decrease and our financial results could be materially adversely affected. In addition, global slowdown in the growth rate of mobile devices will also negatively impact our financial results.
- **Enterprise.** The enterprise storage space is comprised of customers with long design, qualification and test cycles prior to sales. We spend substantial time and resources in our sales process without any assurance that our efforts will produce any customer orders on the timelines or in the quantities we expect. These lengthy and uncertain processes also make it difficult for us to forecast demand and timing of customer orders. Due to longer customer product cycles, we may not be able to transition customers to our leading edge products, which would prevent us from benefitting from the technology transitions that enable cost reductions, which may harm our gross margin. Demand for our enterprise solutions from our hyperscale customers is correlated to large projects and expansions which can be sporadic, resulting in demand that is lumpy and less consistent than the consumer-driven demand for many of our solutions. Hyperscale customers may place orders for significant volumes with short lead times that may be difficult for us to fulfill, and sales to hyperscale customers may negatively impact gross margins due to product mix and pricing, each of which could adversely affect our business. In addition, hyperscale companies may internally develop enterprise storage solutions that reduce the demand for our solutions.
- **Cloud Computing.** Consumers traditionally have stored their data on their PC, often supplemented with personal external storage devices. Most businesses also include similar local storage as a primary or secondary storage location. This storage is typically provided by HDDs and increasingly solid-state drives (“SSDs”). With cloud computing, applications and data are hosted, accessed and processed through a third-party provider over a broadband Internet connection, potentially reducing or eliminating the need for, among other things, significant storage inside the accessing electronic device. Even if we are successful at increasing revenues from sales to cloud computing customers, if we are not successful in manufacturing compelling products to address the cloud computing opportunity, demand for our products in these other markets may decrease and our financial results could be materially adversely affected. Demand for cloud computing solutions themselves may be volatile due to differing patterns of technology adoption and innovation, improved data storage efficiency by cloud computing service providers, and concerns about data protection by end users.
- **Obsolete Inventory.** In some cases, products we manufacture for these markets are uniquely configured for a single customer’s application, creating a risk of obsolete inventory if anticipated demand is not actually realized. In addition, rapid technological change in our industry increases the risk of inventory obsolescence.
- **Macroeconomic Conditions.** Consumer spending has been, and may continue to be, adversely affected in many regions due to negative macroeconomic conditions and high unemployment levels. Please see the risk factor entitled “*Adverse global economic conditions and credit market uncertainty could harm our business, results of operations and financial condition*” for additional risks and uncertainties relating to macroeconomic conditions.

In addition, demand in these areas also could be negatively impacted by developments in the regulation and enforcement of digital rights management and the emergence of new technologies, such as data duplication, compression and storage virtualization. If we are not able to respond appropriately, these factors could lead to our customers' storage needs being satisfied at lower prices with lower capacity hard drives or solid-state storage products, thereby decreasing our revenue or putting us at a disadvantage to competing storage technologies. As a result, even with increasing aggregate demand for digital storage, if we fail to anticipate or timely respond to these developments in the demand for storage, our ASPs could decline, which could adversely affect our operating results and financial condition. Furthermore, our ability to accurately read and respond to market trends, such as trends relating to the Internet of Things or big data, could harm our results.

Deterioration in the PC market may continue or accelerate, which could cause our operating results to suffer.

While sales to non-PC markets are becoming a more significant source of revenue, sales to the PC market remain an important part of our business. We believe that sales of PCs have declined due to fundamental changes in the PC market, including the growth of alternative mobile devices and the lengthening of product life cycles, and that further deterioration of the PC market may continue or accelerate, which could cause our operating results and financial condition to suffer. Additionally, if demand in the PC market is worse than expected as a result of these or other conditions, or demand for our products in the PC market decreases at a faster rate than expected, our operating results and financial condition may be adversely affected.

Selling to the retail market is an important part of our business, and if we fail to maintain and grow our market share or gain market acceptance of our branded products, our operating results could suffer.

Selling branded products is an important part of our business, and as our branded products revenue increases as a portion of our overall revenue, our success in the retail market becomes increasingly important to our operating results. Our success in the retail market depends in large part on our ability to maintain our brand image and corporate reputation and to expand into and gain market acceptance of our products in multiple channels. We must successfully respond to the rapid change away from traditional advertising media, marketing and sales methods to the use of Internet media and advertising, particularly social media, and online sales, or our brand and retail sales could be negatively affected. Adverse publicity, whether or not justified, or allegations of product or service quality issues, even if false or unfounded, could tarnish our reputation and cause our customers to choose products offered by our competitors. In addition, the proliferation of new methods of mass communication facilitated by the Internet makes it easier for false or unfounded allegations to adversely affect our brand image and reputation. If customers no longer maintain a preference for WD, HGST or SanDisk brand products, our operating results may be adversely affected. A significant portion of our sales is made through retailers, and if our retailers are not successful in selling our products, not only would our revenue decrease, but we could also experience lower gross margin due to the return of unsold inventory or the protection we provide to retailers against price declines.

Sales in the distribution channel are important to our business, and if we fail to respond to demand changes in distribution markets or if distribution markets for our products weaken, our operating results could suffer.

Our distribution customers typically sell to small computer manufacturers, dealers, systems integrators and other resellers. We face significant competition in this channel as a result of limited product qualification programs and a significant focus on price and availability of product. In addition, the PC market is experiencing a shift to notebook and other mobile devices and, as a result, more computing devices are being delivered to the market as complete systems, which could weaken the distribution market. If we fail to respond to changes in demand in the distribution market, our operating results could suffer. Additionally, if the distribution market weakens as a result of a slowing PC growth rate, technology transitions or a significant change in consumer buying preference, or if we experience significant price declines due to demand changes in the distribution channel, then our operating results would be adversely affected. Negative changes in the credit-worthiness or the ability to access credit, or the bankruptcy or shutdown of any of our significant retail or distribution partners would harm our revenue and our ability to collect outstanding receivable balances.

Loss of market share with or by a key customer, or consolidation among our customer base, could harm our operating results.

During the three and six months ended December 30, 2016, 43% and 42%, respectively, of our revenue came from sales to our top 10 customers. These customers have a variety of suppliers to choose from and therefore can make substantial demands on us, including demands on product pricing and on contractual terms, often resulting in the allocation of risk to us as the supplier. Our ability to maintain strong relationships with our principal customers is essential to our future performance. If we lose a key customer, if any of our key customers reduce their orders of our products or require us to reduce our prices before we are able to reduce costs, if a customer is acquired by one of our competitors or if a key customer suffers financial hardship, our operating results and financial condition would likely be harmed.

Additionally, if there is consolidation among our customer base, our customers may be able to command increased leverage in negotiating prices and other terms of sale, which could adversely affect our profitability. In addition, if, as a result of increased leverage, customer pressures require us to reduce our pricing such that our gross margins are diminished, it might not be feasible to sell our products to a particular customer, which could result in a decrease in our revenue. Consolidation among our customer base may also lead to reduced demand for our products, replacement of our products by the combined entity with those of our competitors and cancellations of orders, each of which could harm our operating results.

Also, the storage ecosystem is constantly evolving, and our traditional customer base is changing. Fewer companies now hold greater market share for certain applications and services, such as mobile, social media, shopping and streaming media. As a result, the competitive landscape is changing, giving these companies increased leverage in negotiating prices and other terms of sale, which could adversely affect our profitability. In addition, the changes in our evolving customer base create new selling and distribution patterns to which we must adapt. To remain competitive, we must respond to these changes by ensuring we have proper scale in this evolving market, as well as offer products that meet the technological requirements of this customer base at competitive pricing points. To the extent we are not successful in adequately responding to these changes, our operating results and financial condition could be harmed.

Expansion into new markets may increase the complexity of our business, cause us to increase our R&D expenses and investments in manufacturing capability, technology enhancements and go-to-market capability, and if we are unable to successfully adapt our business processes and product offerings as required by these new markets, our ability to grow will be adversely affected.

To remain a significant supplier in the storage industry and to expand into new markets, we will need to offer a broader range of storage products to our customers. We currently offer a variety of 3.5-inch and 2.5-inch hard drives, solid state drives and systems, flash storage solutions, and other products for the PC, mobile, enterprise, data center and other storage markets. As we expand our product lines to sell into new markets, such as our recent entry into active archive systems and new flash memory business through the Merger, including the vertically integrated business model through our ventures with Toshiba Corporation (“Toshiba”) to develop and manufacture NAND flash memory products (“Flash Ventures”), the overall complexity of our business may increase at an accelerated rate and we may become subject to different market dynamics. These dynamics may include, among other things, different demand volume, cyclicity, seasonality, product requirements, sales channels, and warranty and return policies. In addition, expansion into other markets may result in increases in R&D expenses and substantial investments in manufacturing capability, technology enhancements and go-to-market capability. Flash Ventures requires significant investments by both Toshiba and us for technology transitions, including the transition to 3D NAND, and capacity expansions. If we fail to successfully expand into new markets with products that we do not currently offer, we may lose business to our competitors or new entrants who offer these products.

Our vertical integration of recording head and magnetic media manufacturing makes us dependent on our ability to timely and cost-effectively develop recording heads and magnetic media with leading technology and overall quality, increasing capital expenditure costs and asset utilization risks for our business.

We develop and manufacture a substantial portion of the recording heads and magnetic media used in the hard drive products we produce. Consequently, we are more dependent upon our own development and execution efforts and less able to take advantage of recording head and magnetic media technologies developed by other manufacturers. Technology transition for recording heads and magnetic media designs is critical to increasing our volume production of recording heads and magnetic media. We may be unsuccessful in timely and cost-effectively developing and manufacturing recording heads or magnetic media for products using future technologies. We also may not effectively transition our recording head or magnetic media design and technology to achieve acceptable manufacturing yields using the technologies necessary to satisfy our customers' product needs, or we may encounter quality problems with the recording heads or magnetic media we manufacture. If we are unable to timely and cost-effectively develop recording heads and magnetic media with leading technology and overall quality, our ability to sell our products may be significantly diminished, which could materially and adversely affect our business and financial results.

In addition, as a result of our vertical integration of recording heads and magnetic media manufacturing, we make more capital investments and carry a higher percentage of fixed costs than we would if we were not vertically integrated. If our overall level of production decreases for any reason, and we are unable to reduce our fixed costs to match sales, our recording head or magnetic media manufacturing assets may face underutilization that may impact our operating results. We are therefore subject to additional risks related to overall asset utilization, including the need to operate at high levels of utilization to drive competitive costs and the need for assured supply of components that we do not manufacture ourselves. In addition, as a result of adverse labor rates or availability, we may be required to increase investments in automation, which may cause our capital expenditures to increase. If we do not adequately address the challenges related to our recording head or magnetic media manufacturing operations, our ongoing operations could be disrupted, resulting in a decrease in our revenue or profit margins and negatively impacting our operating results.

We make significant investments in R&D to improve our technology and develop new technologies, and unsuccessful investments or investments that are not cost effective could materially adversely affect our business, financial condition and results of operations.

As a leading supplier of hard drives and flash storage solutions, we make significant investments to maintain our existing products and to lead innovation and development of new technologies. This strategy requires us to make significant investments in R&D. In addition, we may increase our capital expenditures and expenses above our historical run-rate model in order to remain competitive or as a result of the Merger with SanDisk, which has historically maintained higher levels of investment in R&D than our company. The current inherent physical limitations associated with storage technologies are resulting in more costly capital expenditures that reduce the cost benefits of technology transitions and could limit our ability to keep pace with reductions in ASPs. These investments may not result in viable technologies or products, and even if they do result in viable technologies or products, they may not be profitable or accepted by the market. Significant investments in unsuccessful or cost-ineffective R&D efforts could materially adversely affect our business, financial condition and results of operations. In addition, increased investments in technology could cause our cost structure to fall out of alignment with demand for our products, which would have a negative impact on our financial results.

Current or future competitors may gain a technology advantage or develop an advantageous cost structure that we cannot match.

It may be possible for our current or future competitors to gain an advantage in product technology, manufacturing technology, or process technology, which may allow them to offer products or services that have a significant advantage over the products and services that we offer. Advantages could be in price, capacity, performance, reliability, serviceability, industry standards or formats, brand and marketing, or other attributes. A competitive cost structure for our products, including critical components, labor and overhead, is also critical to the success of our business. We may be at a competitive disadvantage to any companies that are able to gain a technological or cost structure advantage. The Chinese government and various agencies, state-owned or affiliated enterprises and investment funds are making significant investments to promote China's domestic semiconductor industry consistent with the government's stated national policy objectives. If we are unable to effectively compete with any manufacturers located in China or non-Chinese competitors benefitting from alliances with Chinese companies in the markets where we compete, our operating results and financial condition will suffer.

Consolidation within the data storage industry could provide competitive advantages to our competitors.

The data storage industry as a whole has experienced consolidation over the past several years through acquisitions, mergers and decisions by industry players to exit the industry. Consolidation across the industry, including by our competitors, may enhance their capacity, abilities and resources and lower their cost structure, causing us to be at a competitive disadvantage.

Some of our competitors with diversified business units outside of storage products, may, over extended periods of time, sell storage products at prices that we cannot profitably match.

Some of our competitors earn a significant portion of their revenue from business units outside of storage products. Because they do not depend solely on sales of storage products to achieve profitability, they may sell storage products at lower prices and operate their storage business unit at a loss over an extended period of time while still remaining profitable overall. In addition, if these competitors can increase sales of non-storage products to the same customers, they may benefit from selling their storage products at lower prices. Our operating results may be adversely affected if we cannot successfully compete with the pricing by these companies.

If we fail to qualify our products and achieve design wins with our customers, it may have a significant adverse impact on our sales and margins.

We regularly engage in new product qualification with our customers, and the product qualification process may be lengthy for some customers, including those in enterprise storage. Once a product is accepted for qualification testing, failures or delays in the qualification process can result in delayed or reduced product sales, reduced product margins caused by having to continue to offer a more costly current generation product, or lost sales to that customer until the next generation of products is introduced. The effect of missing a product qualification opportunity is magnified by the limited number of high volume OEMs and hyperscale customers, which continue to consolidate their share of the storage markets. Likewise, if product life cycles lengthen, we may have a significantly longer period to wait before we have an opportunity to qualify a new product with a customer, which could reduce our profits because we expect declining gross margins on our current generation products as a result of competitive pressures. Even if our products meet customer specifications, our sales to these customers are dependent upon the customers choosing our products over those of our competitors and purchasing our products in sufficient volume, our ability to supply our products in sufficient quantity and in a timely manner and, with respect to OEM partners, the OEMs' ability to create, market and successfully sell products containing our solutions. Moreover, in transitioning to new technologies, such as 3D NAND, and products, we may not achieve design wins, our customers may delay transition to these new technologies, our competitors may transition more quickly than we do, or we may experience product delays, cost overruns or performance issues that could harm our operating results and financial condition.

We are subject to risks related to product defects or the unintended use or security breaches of our products, which could result in product recalls or epidemic failures and could subject us to warranty claims in excess of our warranty provisions or which are greater than anticipated, litigation or indemnification claims.

We warrant the majority of our products for periods of one to five years. We test our products in our manufacturing facilities through a variety of means. However, our testing may fail to reveal defects in our products that may not become apparent until after the products have been sold into the market. In addition, our products may be used in a manner that is not intended or anticipated by us, resulting in potential liability. Accordingly, there is a risk that product defects will occur, which could require a product recall. Product recalls can be expensive to implement. As part of a product recall, we may be required or choose to replace the defective product. Moreover, there is a risk that product defects may trigger an epidemic failure clause in a customer agreement. If an epidemic failure occurs, we may be required to replace or refund the value of the defective product and to cover certain other costs associated with the consequences of the epidemic failure. In addition, product defects, product recalls or epidemic failures may cause damage to our reputation or customer relationships, lost revenue, indemnification for a recall of our customers' products, warranty claims, litigation or loss of market share with our customers, including our OEM and original design manufacturers ("ODM") customers. Our business liability insurance may be inadequate or future coverage may be unavailable on acceptable terms, which could adversely impact our operating results and financial condition.

Our standard warranties contain limits on damages and exclusions of liability for consequential damages and for misuse, improper installation, alteration, accident or mishandling while in the possession of someone other than us. We record an accrual for estimated warranty costs at the time revenue is recognized. We may incur additional expenses if our warranty provision do not reflect the actual cost of resolving issues related to defects in our products, whether as a result of a product recall, epidemic failure or otherwise. If these additional expenses are significant, it could adversely affect our business, financial condition and operating results.

Certain of our products contain encryption or security algorithms to protect third party content and user-generated data stored on our products. To the extent our products are hacked or the encryption schemes are compromised or breached, this could harm our business by hurting our reputation, requiring us to employ additional resources to fix the errors or defects and expose us to litigation and indemnification claims.

In addition, third-party components or applications that we incorporate or use in our products may contain defects in design or manufacturing that could unexpectedly result in epidemic failures and subject us to liability.

We rely substantially on our business ventures and strategic partnerships with Toshiba for the supply of NAND flash memory, which subjects us to risks and uncertainties that could harm our business, financial condition and operating results.

We are dependent on Flash Ventures and other strategic relationships with Toshiba for our NAND flash memory supply, and therefore our business, financial condition and operating results, and our ability to realize the anticipated benefits from the Merger, will be dependent on the success of Flash Ventures and other strategic relationships with Toshiba.

A majority of our NAND flash memory is supplied by Flash Ventures, which limits our ability to respond to demand and supply changes. A failure to accurately forecast demand could cause us to over-invest or under-invest in technology transitions or the expansion of captive memory capacity in Flash Ventures. Over-investment could result in excess supply, which could cause significant decreases in our product prices, significant excess, obsolete or lower of cost or net realizable value inventory write-downs or under-utilization charges, and the potential impairment of our investments in Flash Ventures. On the other hand, if we or Toshiba under-invest in captive memory capacity or technology transitions, if we grow capacity more slowly than the rest of the industry, if our technology transitions do not occur on the timeline that we expect, if we encounter unanticipated difficulties in implementing these transitions, or if we implement technology transitions more slowly than our competitors, we may not have enough captive supply of the right type of memory or at all to meet demand on a timely and cost effective basis and we may lose opportunities for revenue, gross margin and share as a result. If our NAND memory supply is limited, we may make strategic decisions with respect to the allocation of our supply among our products and customers, and these strategic allocation decisions may result in less favorable gross margin in the short term or damage certain customer relationships. Growth of our NAND flash memory bit supply at a slower rate than the overall industry for an extended period of time would result in lowering our share which could limit our future opportunities and harm our financial results. We are also contractually obligated to pay for 50% of the fixed costs of Flash Ventures regardless of whether we purchase any wafers from Flash Ventures. Furthermore, purchase orders placed with Flash Ventures and under the foundry arrangements with Toshiba for up to three months are binding and cannot be canceled. Therefore, once our purchase decisions have been made, our production costs for flash memory are fixed, and we may be unable to reduce costs to match any subsequent declines in pricing or demand, which would harm our gross margin. Our limited ability to react to fluctuations in flash memory supply and demand makes our financial results particularly susceptible to variations from our forecasts and expectations.

In addition, we partner with Toshiba on the development of NAND flash technology, including the next technology transitions of NAND flash, as well as other non-volatile memory technology.

These ventures and strategic partnerships are subject to various risks that could harm the value of our investments, our revenue and costs, our future rate of spending, our technology plans and our future growth opportunities. Under the terms of our venture agreements with Toshiba, which govern the operations of Flash Ventures, we have limited power to unilaterally direct most of the activities that most significantly impact Flash Ventures' performance. Although SanDisk and Toshiba have a long history of aligning on important manufacturing and technology development decisions, the integration of SanDisk into our organization could complicate the process of reaching agreement with Toshiba in a timely and favorable manner. We may not always agree with Toshiba on our joint R&D roadmap or expansions or conversions of production capacity. A change in the management or control of Toshiba's storage business could lead to delays in decision-making or changes in strategic direction that could also adversely impact Flash Ventures. In addition, Toshiba's financial position or shift in strategic priorities could adversely impact our business.

Flash Ventures requires significant investments by both Toshiba and us for technology transitions, including the transition to 3D NAND, and capacity expansions. In March 2016, Toshiba announced plans to construct a new wafer fab in Yokkaichi, Japan, to provide additional cleanroom space for expanded 3D NAND production. Although we intend to extend the joint venture partnership with Toshiba to the new wafer fab, there is no certainty as to when, and on what terms, we will participate with Toshiba in any investment in, or use of, the new wafer fab, if at all. Failure to extend the joint venture partnership or failure to continue to secure and invest in additional cleanroom space to support the continued 3D NAND transition could adversely impact our supply of captive NAND flash memory and financial results. If Toshiba does not or we do not provide sufficient resources or have adequate access to credit, investments in Flash Ventures could be delayed or reduced. In addition, in the event that lease financings for Flash Ventures are not available on favorable terms or at all, more cash would be required to fund these investments.

Our strategic relationships subject us to risks that could adversely affect our business, financial condition and results of operations.

We have entered into strategic relationships with various partners for future product development, sales growth and the supply of technologies, components, equipment and materials for use in our product design and manufacturing, including our relationships with Toshiba for NAND flash memory supply. In addition, in the first quarter of 2017, our joint venture with Unisplendour Corporation Limited (“Unis”) to market and sell our current data center storage systems in China and to develop data storage systems for the Chinese market in the future became operational; the joint venture is 49% owned by us and 51% owned by Unis and its subsidiary, Unisoft (Wuxi) Group Co. Ltd. Please see the risk factor entitled “*Because we are dependent on a limited number of qualified suppliers for components, sub-assemblies, testing, equipment, consumables, raw materials, and logistics, a supplier’s inability, unwillingness, or failure to support us in a timely manner with goods or services at a quality level and cost acceptable to us can adversely affect our margins, revenues and operating results,*” for a further description of the risks associated with our reliance on external suppliers. These strategic relationships are subject to various risks that could adversely affect the value of our investments and our results of operations and financial condition. These risks include, but are not limited to, the following:

- our interests could diverge from our partners’ interests or we may not agree with co-venturers on ongoing activities, technology transitions or on the amount, timing or nature of further investments in the relationship;
- we may experience difficulties and delays in ramping production at, and transferring technology to, our business ventures;
- our control over the operations of our business ventures is limited;
- due to financial constraints, our co-venturers may be unable to meet their commitments to us or may pose credit risks for our transactions with them;
- due to differing business models, financial constraints or long-term business goals, our partners may decide not to join us in funding capital investment by our business ventures, which may result in higher levels of cash expenditures by us or prevent us from proceeding in the investment;
- we may lose the rights to technology or products being developed by the strategic relationship, including if any of our co-venturers is acquired by another company, files for bankruptcy or experiences financial or other losses;
- a bankruptcy event involving a co-venturer could result in the early termination or adverse modification of the business venture or agreements governing the business venture;
- we may experience difficulties or delays in collecting amounts due to us from our co-venturers;
- the terms of our arrangements may turn out to be unfavorable; and
- changes in tax, legal or regulatory requirements may necessitate changes in the agreements with our co-venturers.

If our strategic relationships are unsuccessful or there are unanticipated changes in, or termination of, our strategic relationships, our business, results of operations and financial condition may be adversely affected.

Because we are dependent on a limited number of qualified suppliers for components, sub-assemblies, testing, equipment, consumables, raw materials, and logistics, a supplier's inability, unwillingness, or failure to support us in a timely manner with goods or services at a quality level and cost acceptable to us can adversely affect our margins, revenues and operating results.

We depend on an external supply base for technologies, software (including firmware), controller, components, equipment and materials for use in our product design and manufacturing. We also depend on suppliers for a portion of our wafer testing, chip assembly, product assembly and product testing, and on service suppliers for providing technical support for our products. In addition, we use logistics partners to manage our just-in-time hubs, distribution centers and freight from suppliers to our factories and from our factories to our customers throughout the world. Many of the components and much of the equipment we acquire must be specifically designed to be compatible for use in our products or for developing and manufacturing our future products, and are only available from a limited number of suppliers, some of whom are our sole-source suppliers. We are therefore dependent on these suppliers to be able and willing to dedicate adequate engineering resources to develop components that can be successfully integrated into our products, technology and equipment that can be used to develop and manufacture our next-generation products efficiently. Our supply base has experienced industry consolidation. Where we rely on a limited number of suppliers or a single supplier, the risk of supplier loss due to industry consolidation is enhanced. Any disruption in our supply chain could reduce our revenue and adversely impact our financial results.

From time to time, our suppliers have experienced difficulty meeting our requirements. If we are unable to purchase sufficient quantities from our current suppliers or qualify and engage additional suppliers, we may not be able to meet demand for our products. We do not have long-term contracts with some of our existing suppliers, nor do we always have guaranteed manufacturing capacity with our suppliers and, therefore, we cannot guarantee that they will devote sufficient resources or capacity to manufacturing our products. We are not able to directly control product delivery schedules or quality assurance. Furthermore, we manufacture on a turnkey basis with some of our suppliers. In these arrangements, we do not have visibility and control of our suppliers' inventories of purchased parts necessary to build our products or of the progress of our products through their assembly line. Any significant problems that occur at our suppliers, or their failure to perform at the level we expect, could lead to product shortages or quality assurance problems, either of which would harm our operating results and financial condition. In addition, if we are unable to purchase sufficient quantities from our current suppliers, we may not be able to engage alternative suppliers who are able or willing to provide goods or services in sufficient quantities or at a cost acceptable to us.

Our products require controllers and firmware. We rely on a limited number of third-party vendors to develop or supply controllers for many of our high-value solutions. Any delays or cost increases in developing or sourcing controllers or firmware, or incompatibility or quality issues relating to the controllers or firmware in our products, could harm our financial results as well as business relationships with our customers.

A majority of our flash memory is currently supplied by Flash Ventures and, to a much lesser extent, by third-party silicon suppliers. Any disruption or shortage in supply of flash memory from our captive or non-captive sources would harm our operating results and financial condition. Many of the risks that affect us also affect our supply base and Flash Ventures, including, but not limited to, having single site manufacturing locations and other facilities based in high risk regions of the world (for example, Flash Ventures is located in Yokkaichi, Japan), natural disasters, power shortages, macro and local economic conditions, shortages of commodity materials, proper management of technology transitions, geo-political risks, employee strikes and other labor actions, compliance with legal requirements, financial instability and exposure to intellectual property ("IP") and other litigation, including an injunction or other action that could delay shipping. If any of these risks were to affect our suppliers or Flash Ventures, we could also be adversely affected, especially in the case of products, components or services that are single-sourced. For example, if suppliers are facing increased costs due to the above risks, they may require us to enter into long-term volume agreements to shift the burden of fixed costs to us. Further, we work closely with many of our suppliers and strategic partners to develop new technologies and, as a result, we may become subject to litigation from our suppliers, strategic partners or third parties.

Without a capable and financially stable supply base that has established appropriate relationships within the supply chain and has implemented business processes, strategies and risk management safeguards, we would be unable to develop our products, manufacture them in high volumes, and distribute them to our customers to execute our business plans effectively. Some of our suppliers have also experienced a decline in financial performance. Our suppliers may be acquired by our competitors, consolidate, or decide to exit the industry, redirect their investments and increase costs to us, each of which may have an adverse effect on our business and operations. In addition, moving to new technologies may require us to align to, and build, a new supply base. Our success in new product areas may be dependent on our ability to develop close relationships with new suppliers, with preferential agreements. Where this cannot be done, our business and operations may be adversely affected.

In addition to an external supply base, we also rely on an internal supply chain of heads, media and media substrate, and we rely on our business ventures with Toshiba for the supply of NAND flash memory. Please see the risk factors entitled, “*A fundamental change in storage technologies and standards could result in significant increases in our costs and could put us at a competitive disadvantage,*” “*If we do not properly manage technology transitions, our competitiveness and operating results may be negatively affected,*” and “*We rely substantially on our business ventures and strategic partnerships with Toshiba for the supply of NAND flash memory, which subjects us to risks and uncertainties that could harm our business, financial condition and operating results*” for a review of some of the risks related to these supplies.

Price volatility, shortages of critical materials or components, or use by other industries of materials and components used in the storage industry, may negatively impact our operating results.

Increases in the cost for certain critical materials and components and oil may increase our costs of manufacturing and transporting our products and key components and may result in lower operating margins if we are unable to pass these increased costs on to our customers. Shortages of critical components such as DRAM and NAND flash, or materials such as glass substrates, stainless steel, aluminum, nickel, neodymium, ruthenium, platinum or cerium, may increase our costs and may result in lower operating margins if we are unable to find ways to mitigate these increased costs. We or our suppliers acquire certain precious metals and rare earth metals like ruthenium, platinum, neodymium and cerium, which are critical to the manufacture of components in our products from a number of countries, including the People’s Republic of China. The government of China or any other nation may impose regulations, quotas or embargoes upon these metals that would restrict the worldwide supply of such metals or increase their cost, both of which could negatively impact our operating results until alternative suppliers are sourced. Furthermore, if other high volume industries increase their demand for materials or components used in our products, our costs may further increase, which could have an adverse effect on our operating margins. In addition, shortages in other components and materials used in our customers’ products could result in a decrease in demand for our products, which would negatively impact our operating results.

Contractual commitments with component suppliers may result in us paying increased charges and cash advances for such components or may cause us to have inadequate or excess component inventory.

To reduce the risk of component shortages, we attempt to provide significant lead times when buying components, which may subject us to cancellation charges if we cancel orders as a result of technology transitions or changes in our component needs. In addition, we may from time to time enter into contractual commitments with component suppliers in an effort to increase and stabilize the supply of those components and enable us to purchase such components at favorable prices. Some of these commitments may require us to buy a substantial number of components from the supplier or make significant cash advances to the supplier; however, these commitments may not result in a satisfactory increase or stabilization of the supply of such components. Furthermore, as a result of uncertain global economic conditions, our ability to forecast our requirements for these components has become increasingly difficult, therefore increasing the risk that our contractual commitments may not meet our actual supply requirements, which could cause us to have inadequate or excess component inventory and adversely affect our operating results and increase our operating costs.

If we do not properly manage technology transitions, our competitiveness and operating results may be negatively affected.

The storage markets in which we offer our products continuously undergo technology transitions that we must anticipate and adapt our products to address in a timely manner. If we fail to implement new technologies successfully, or if we are slower than our competitors at implementing new technologies, we may not be able to competitively offer products that our customers desire or keep pace with ASP reduction, which could harm our operating results. In addition, if our customers choose to delay transition to new technologies, if demand for the products that we develop is lower than expected or if the supporting technologies to implement these new technologies are not available, we may be unable to achieve the cost structure required to support our profit objectives or may be unable to grow or maintain our market position.

Our successful development of 3D NAND and other non-volatile memory technologies, such as 3D resistive random-access memory (“ReRAM”), and transitioning our customers to these technologies in a timely and effective manner are crucial to continuing the cost reductions necessary to maintain adequate gross margin. In transitioning our 2D NAND manufacturing capacity to 3D NAND technology, we could experience delays or other challenges in the production ramp, qualification of wafers, shipment of samples to customers or customer approval process. 3D NAND and any new manufacturing node may be more susceptible to manufacturing yield issues. Manufacturing yield issues may not be identified during the development or production process or solved until an actual product is manufactured and tested, further increasing our costs. If our technology transitions, including the production ramp of 3D NAND technology, take longer, are more costly to complete than anticipated, or do not improve manufacturing yield or other manufacturing efficiencies, our flash memory costs may not remain competitive with other NAND flash memory producers or may not fall commensurate with declines in the price of NAND flash memory, which would harm revenues, our gross margin and operating results.

Many companies, including some of our competitors, have developed or are attempting to develop alternative non-volatile technologies. Successful broad-based commercialization of one or more competing technologies, as well as differing strategies and timing with respect to the transition from 2D NAND to 3D NAND, could reduce the competitiveness and future revenue and profitability of our 2D NAND and 3D NAND flash technologies, and the potential 3D ReRAM technology that we are developing with our partners. In addition, we generate license and royalty revenue from NAND flash technology, and if NAND flash technology is replaced by a technology where our IP is less relevant, our license and royalty revenue would decrease. Also, we may not have access to alternative technologies that we do not develop internally and we may have to pay royalties in order to access such technologies.

Changes in product life cycles could adversely affect our financial results.

If product life cycles lengthen, we may need to develop new technologies or programs to reduce our costs on any particular product to maintain competitive pricing for that product. Longer product life cycles could also restrict our ability to transition customers to our newer products in a timely manner, or at all, negatively impacting our ability to recoup our significant R&D investments to improve our existing technology and develop new technologies. If product life cycles shorten, it may result in an increase in our overall expenses and a decrease in our gross margins, both of which could adversely affect our operating results. In addition, shortening of product life cycles also makes it more difficult to recover the cost of product development before the product becomes obsolete. Our failure to recover the cost of product development in the future could adversely affect our operating results.

A fundamental change in storage technologies and standards could result in significant increases in our costs and could put us at a competitive disadvantage.

Historically, when the industry experiences a fundamental change in storage technologies or standards, any manufacturer that fails to successfully and timely adjust its designs and processes to accommodate the new technology or standard fails to remain competitive. There are some revolutionary technologies, such as current-perpendicular-to-plane giant magnetoresistance, shingle magnetic recording, heat-assisted magnetic recording, patterned magnetic media and advanced signal processing that, if implemented by a competitor on a commercially viable basis ahead of the industry, could put us at a competitive disadvantage. In addition, many companies, including some of our competitors, have developed or are attempting to develop alternative non-volatile technologies, including non-NAND technologies such as magnetoresistive random-access memory (“RAM”), ReRAM, 3D XPoint, phase change and Memristor, as well as NAND based vertical or stacked 3D memories based on charge trap, floating gate and other cell architecture. In embedded solutions, certain competitors have recently introduced a mobile storage standard referred to as Universal Flash Storage (“UFS”). In the data center market, certain competitors have recently introduced a non-volatile memory express (“NVMe”) product that can be used as a substitute for our peripheral component interconnect express (“PCIe”) solutions. In addition, a provider of processors and non-volatile memory solutions may be developing a new standard to attach ultra-low latency non-volatile memory to its processor memory bus, which it may choose not to license to its competitors, resulting in it being a single source provider of such non-volatile memory solutions. As a result of these shifts in technology and standards, we could incur substantial costs in developing new technologies, such as recording heads, magnetic media and tools, in adopting new standards or in investing in different capital equipment or manufacturing processes to remain competitive. If we fail to successfully implement these new technologies or standards, or if we are significantly slower than our competitors at implementing new technologies or standards, we may not be able to offer products with capacities and capabilities that our customers desire, which could harm our operating results.

The difficulty of introducing hard drives with higher levels of areal density and the challenges of reducing other costs may impact our ability to achieve historical levels of cost reduction.

Storage capacity of the hard drive, as manufactured by us, is determined by the number of disks and each disk’s areal density. Areal density is a measure of the amount of magnetic bits that can be stored on the recording surface of the disk. Generally, the higher the areal density, the more information can be stored on a single platter. Higher areal densities require existing recording head and magnetic media technology to be improved or new technologies developed to accommodate more data on a single disk. Historically, we have been able to achieve a large percentage of cost reduction through increases in areal density. Increases in areal density mean that the average drive we sell has fewer heads and disks for the same capacity and, therefore, may result in a lower component cost. However, increasing areal density has become more difficult in the storage industry. If we are not able to increase areal density at the same rate as our competitors or at a rate that is expected by our customers, we may be required to include more components in our drives to meet demand without corresponding incremental revenue, which could negatively impact our operating margins and make achieving historical levels of cost reduction difficult or unlikely. Additionally, increases in areal density may require us to make further capital expenditures on items such as new test equipment needed as a result of an increased number of gigabytes per platter. Our inability to achieve cost reductions could adversely affect our operating results.

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Our license and royalty revenue may fluctuate or decline significantly in the future due to license agreement expirations or renewals, declines in sales of the products or use of technology underlying the license and royalty revenue by our licensees, or if licensees fail to perform on a portion or all of their contractual obligations.

If our existing licensees do not renew their licenses upon expiration, renew or sign new agreements on less favorable terms, exercise their option to terminate the license or fail to exercise their option to extend the licenses, or we are not successful in signing new licensees in the future, our license revenue, profitability and cash provided by operating activities would be harmed and we may incur significant patent litigation costs to enforce our patents against these licensees. As our older patents expire, and the coverage of our newer patents may be different, it may be more difficult to negotiate or renew favorable license agreement terms or a license agreement at all. Our agreements may require us in certain instances to recognize license revenue related to a particular licensee all in one period instead of over time, which could create additional volatility in our licensing revenue. A portion of our license and royalty revenue is based on sales of product categories as well as the underlying technology, and fluctuations in the sales of those products or technology adoption rates would also result in fluctuations in the license and royalty revenue due to us under our agreements. If our licensees or we fail to perform on contractual obligations, we may incur costs to enforce or defend the terms of our licenses and there can be no assurance that our enforcement, defense or collection efforts will be effective. If we license new IP from third parties or existing licensees, we may be required to pay license fees, royalty payments or offset existing license revenue. We may enter into agreements with customers, suppliers or partners that could limit our ability to monetize our IP or could result in us being required to provide IP indemnification to our customers, suppliers or partners. In addition, we may be subject to disputes, claims or other disagreements on the timing, amount or collection of royalties or license payments under our license agreements.

If we do not properly manage new product development, our competitiveness and operating results may be negatively affected.

Our success depends in part on our ability to develop and introduce new products in a timely manner in order to keep pace with technology advancements. Advances in semiconductor technology have resulted in other emerging technologies that can be competitive with traditional storage technologies. We may be unsuccessful in anticipating and developing new and improved products for the client, enterprise and other storage markets in response to competing technologies. If our hard drive, solid state products and our storage solutions products fail to offer a superior value proposition to alternative storage products, we will be at a competitive disadvantage and our business will suffer. In some cases, our customers' demand for a more diversified portfolio results in investments in new products for a particular market that do not necessarily expand overall market opportunity, which may negatively affect our operating results. As we introduce new products, standards or technologies, it can take time for these new standards or technologies to be adopted, for consumers to accept and transition to these new standards or technologies and for significant sales to be generated, if at all. Failure of consumers or enterprises to adopt our new products, standards or technologies could harm our results of operations as we fail to reap the benefits of our investments.

In addition, the success of our new product introductions depends on a number of other factors, including:

- difficulties faced in manufacturing ramp;
- implementing at an acceptable cost product features expected by our customers;
- market acceptance/qualification;
- effective management of inventory levels in line with anticipated product demand;
- quality problems or other defects in the early stages of new product introduction and problems with compatibility between our products and those of our customers that were not anticipated in the design of those products;
- our ability to increase our software development capability; and
- the effectiveness of our go-to-market capability in selling these new products.

In particular, as part of our growth strategy, we have made significant investments in active archive systems, which are designed to enable organizations to rapidly access massive long-term data stores. For example, our acquisition of Amplidata NV in March 2015 was partially driven by our strategy to expand in this area. We expect to continue to make significant investments in active archive systems. Our active archive systems may fail to gain market acceptance, or the market for active archive systems may not grow as we anticipate.

We have also seen, and anticipate continuing to see, an increase in customers requesting that we develop products, including software associated with our products, that incorporate open source software elements and operate in an open source environment. Adapting to this demand may cause product delays, placing us at a competitive disadvantage. Open source products could also reduce our capability for product differentiation or innovation and our affected products could be diminished to commodity status, which we expect would place increased downward pressure on our margins. If we fail to successfully anticipate and manage issues associated with our product development generally, our business may suffer.

Our operations, and those of certain of our suppliers and customers, are concentrated in large, purpose-built facilities, subjecting us to substantial risk of damage or loss if operations at any of these facilities are disrupted.

As a result of our cost structure and strategy of vertical integration, we conduct our operations at large, high volume, purpose-built facilities in California and throughout Asia. The concentration of Flash Ventures in Yokkaichi, Japan, magnifies the risks of supply disruption. The facilities of many of our customers, our suppliers and our customers' suppliers are also concentrated in certain geographic locations throughout Asia and elsewhere. A localized health risk affecting our employees at these facilities or the staff of our or our customers' other suppliers, such as the spread of a pandemic influenza, could impair the total volume of our products that we are able to manufacture or sell, which would result in substantial harm to our operating results. Similarly, a fire, flood, earthquake, tsunami or other natural disaster, condition or event such as political instability, civil unrest or a power outage that adversely affects any of these facilities, including access to or from these facilities by employees or logistics operators, would significantly affect our ability to manufacture or sell our products, which would result in a substantial loss of sales and revenue and a substantial harm to our operating results. For example, prior to the 2011 flooding in Thailand, all of our internal slider capacity and 60% of our hard drive manufacturing capacity was in Thailand. As a result of the flooding in Thailand, our facilities were inundated and temporarily shut down. During that period, our ability to manufacture hard drives was significantly constrained, adversely affecting our business, financial condition and results of operations. In addition, the concentration of our manufacturing sites could exacerbate the negative impacts resulting from localized labor unrest or other employment issues. A significant event that impacts any of our manufacturing sites, or the sites of our customers or suppliers, could adversely affect our ability to manufacture or sell our products, and our business, financial condition and results of operations could suffer.

We may incur losses beyond the limits of, or outside the scope of, the coverage of our insurance policies. There can be no assurance that in the future we will be able to maintain existing insurance coverage or that premiums will not increase substantially. Due to market availability, pricing or other reasons, we may elect not to purchase insurance coverage or to purchase only limited coverage. We maintain limited insurance coverage and, in some cases, no coverage at all, for natural disasters and environmental damages, as these types of insurance are sometimes not available or available only at a prohibitive cost. We depend upon Toshiba to obtain and maintain sufficient property, business interruption and other insurance for Flash Ventures. If Toshiba fails to do so, we could suffer significant unreimbursable losses, and such failure could also cause Flash Ventures to breach various financing covenants.

Manufacturing, marketing and selling our products globally subjects us to numerous risks.

Currently, a large portion of our revenue is derived from our international operations, and many of our products and components are produced overseas. Our revenue and future growth is significantly dependent on the growth of international markets, and we may face difficulties in entering or maintaining international sales markets. We are subject to risks associated with our global manufacturing operations and global marketing and sales efforts, as well as risks associated with our utilization of and reliance on contract manufacturers, including:

- obtaining requisite governmental permits and approvals, compliance with foreign laws and regulations, changes in foreign laws and regulations;
- the need to comply with regulations on international business, including the Foreign Corrupt Practices Act, the United Kingdom Bribery Act 2010, the anti-bribery laws of other countries and rules regarding conflict minerals;
- currency exchange rate fluctuations or restrictions;
- political and economic instability, civil unrest and natural disasters;
- limited transportation availability, delays, and extended time required for shipping, which risks may be compounded in periods of price declines;
- higher freight rates;
- labor challenges, including difficulties finding and retaining talent or responding to labor disputes or disruptions;
- trade restrictions or higher tariffs and fees;
- import and export restrictions and license and certification requirements, including on encryption technology, and complex customs regulations;
- copyright levies or similar fees or taxes imposed in European and other countries;
- exchange, currency and tax controls and reallocations;
- increasing labor and overhead costs;
- weaker protection of IP rights;
- difficulties in managing international operations, including appropriate internal controls; and
- loss or non-renewal of favorable tax treatment under agreements or treaties with foreign tax authorities.

As a result of these risks, our business, results of operations or financial condition could be adversely affected. Some of these risks, such as trade restrictions, higher tariffs and fees, import and export restrictions or loss of favorable tax treatment under agreements or treaties with foreign tax authorities, could increase as a result of changes to policies, rules and regulations which may be proposed or implemented by the new U.S. President and his administration.

Terrorist attacks may adversely affect our business and operating results.

Recent terrorist incidents around the world and the continued threat of terrorist activity and other acts of war or hostility have created uncertainty in the financial and insurance markets and have significantly increased the political, economic and social instability in some of the geographic areas in which we, our suppliers or our customers operate. Additionally, it is uncertain what impact the reactions to such acts by various governmental agencies and security regulators worldwide will have on shipping costs. Acts of terrorism, either domestically or abroad, could create further uncertainties and instability. To the extent this results in disruption or delays of our manufacturing capabilities, R&D activities (including our operations in Israel) or shipments of our products, our business, operating results and financial condition could be adversely affected. Any of these events could also increase volatility in the U.S. and world financial markets, which could have a negative effect on our stock price and may limit the capital resources available to us and our customers or suppliers, or adversely affect consumer confidence.

Sudden disruptions to the availability of air transportation, or ocean or land freight lanes, could have an impact on our operations.

We generally ship our products to our customers, and receive shipments from our suppliers, via air, ocean or land freight. The sudden unavailability or disruption of air transportation, cargo operations or ocean, rail or truck freight lanes caused by, among other things, labor difficulties or disputes, severe weather patterns or other natural disasters, or political instability or civil unrest, could impact our operating results by impairing our ability to timely and efficiently receive shipments from our suppliers or deliver our products.

If our technology infrastructure, systems or products are compromised, damaged or interrupted by cyber attacks, data security breaches, other security problems, security vulnerabilities or design defects, or sustain system failures, our operating results and financial condition could be adversely affected.

We experience cyber attacks of varying degrees on our technology infrastructure and systems and, as a result, unauthorized parties have obtained in the past, and may in the future obtain, access to our computer systems and networks. The technology infrastructure and systems of our suppliers, vendors and partners may also experience such attacks. Cyber attacks can include computer viruses, computer denial-of-service attacks, worms, and other malicious software programs or other attacks, covert introduction of malware to computers and networks, impersonation of authorized users, and efforts to discover and exploit any security vulnerabilities or security weaknesses, as well as intentional or unintentional acts by employees or other insiders with access privileges, intentional acts of vandalism by third parties and sabotage. We believe cyber attack attempts are increasing in number and that cyber attackers are developing increasingly sophisticated systems and means to not only attack systems, but also to evade detection or to obscure their activities. Our products are also targets for cyber attacks. While some of our products contain encryption or security algorithms to protect third-party content or user-generated data stored on our products, these products could still be hacked or the encryption schemes could be compromised, breached, or circumvented by motivated and sophisticated attackers. We have agreed with certain customers and strategic partners, including Toshiba, to undertake certain commitments to promote information security, and we may be liable to Toshiba or such other parties if we fail to meet our cyber security commitments.

In addition, our technology infrastructure and systems are vulnerable to damage or interruption from natural disasters, power loss and telecommunications failures. Further, our products contain sophisticated hardware and operating system software and applications that may contain security problems, security vulnerabilities, or defects in design or manufacture, including “bugs” and other problems that could interfere with the intended operation of our products.

If efforts to breach our infrastructure, systems or products are successful or we are unable to protect against these risks, we could suffer interruptions, delays, or cessation of operations of our systems, and loss or misuse of proprietary or confidential information, IP, or sensitive or personal information. Breaches of our infrastructure, systems or products could also cause our customers and other affected third parties to suffer loss or misuse of proprietary or confidential information, IP, or sensitive or personal information, and could harm our relationships with customers and other third parties. As a result, we could experience additional costs, indemnification claims, litigation, and damage to our brand and reputation. All of these consequences could harm our reputation and our business and materially and adversely affect our operating results and financial condition.

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If we fail to identify, manage, complete and integrate acquisitions, investment opportunities or other significant transactions, which are a key part of our growth strategy, it may adversely affect our future results.

We seek to be an industry-leading developer, manufacturer and provider of innovative storage solutions, balancing our core hard drive and flash memory business with growing investments in newer areas that we believe will provide us with higher growth opportunities. Acquisitions of, investment opportunities in, or other significant transactions with companies that are complementary to our business are a key part of our overall business strategy. For example, we have completed the acquisitions of SanDisk (in May 2016), Amplidata NV (in March 2015), Virident Systems, Inc. (in October 2013) and sTec, Inc. (in September 2013). In order to pursue this part of our growth strategy successfully, we must continue to identify attractive acquisition or investment opportunities, successfully complete the transactions, some of which may be large and complex, and manage post-closing issues such as integration of the acquired company or employees. We may not be able to continue to identify or complete appealing acquisition or investment opportunities given the intense competition for these transactions. We are also subject to certain covenants in our debt agreements which place limits on our ability to complete acquisitions and investments. Even if we identify and complete suitable corporate transactions, we may not be able to successfully address any integration challenges in a timely manner, or at all. Failing to successfully integrate or realign our business to take advantage of efficiencies or reduce redundancies of an acquisition may result in not realizing all or any of the anticipated benefits of the acquisition. In addition, failing to achieve the financial model projections for an acquisition may result in the incurrence of impairment charges and other expenses, both of which could adversely impact our results of operations or financial condition. Acquisitions and investments may also result in the issuance of equity securities that may be dilutive to our shareholders and the issuance of additional indebtedness which would put additional pressure on liquidity. Furthermore, we may agree to provide continuing service obligations or enter into other agreements in order to obtain certain regulatory approvals of our corporate transactions, and failure to satisfy these additional obligations could result in our failing to obtain regulatory approvals or the imposition of additional obligations on us, any of which could adversely affect our business, financial condition and results of operations.

The loss of our key executive management, staff and skilled employees, the inability to hire and integrate new employees or decisions to realign our business could negatively impact our business prospects.

Our success depends upon the continued contributions of our key management, staff and skilled employees, many of whom would be extremely difficult to replace. Global competition for skilled employees in the data storage industry is intense and, as we attempt to move to a position of technology leadership in the storage industry, our business success becomes increasingly dependent on our ability to retain our key staff and skilled employees, to attract, integrate and retain new skilled employees, including employees from acquisitions, and to make decisions to realign our business to take advantage of efficiencies or reduce redundancies. Volatility or lack of positive performance in our stock price and the overall markets may adversely affect our ability to retain key staff or skilled employees who have received equity compensation. Additionally, because a substantial portion of our key employees' compensation is placed "at risk" and linked to the performance of our business, when our operating results are negatively impacted, we are at a competitive disadvantage for retaining and hiring key management, staff and skilled employees versus other companies that pay a relatively higher fixed salary. If we lose our existing key management, staff or skilled employees, or are unable to hire and integrate new key management, staff or skilled employees, or if we fail to implement succession plans for our key management or staff, our operating results would likely be harmed. Furthermore, if we do not realize the anticipated benefits of our intended realignment after we make decisions regarding our personnel and implement our realignment plans, our operating results could be adversely affected.

We and certain of our officers are at times involved in litigation, including IP, antitrust and securities litigation, which may be costly, may divert the efforts of our key personnel and could result in adverse court rulings, which could materially harm our business.

We are involved in litigation, including cases involving our IP rights and those of others, antitrust and commercial matters, putative securities class action suits and other actions. We are the plaintiff in some of these actions and the defendant in others. Some of the actions seek injunctive relief, including injunctions against the sale of our products and substantial monetary damages, which if granted or awarded, could materially harm our business, financial condition and operating results.

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Litigation is subject to inherent risks and uncertainties that may cause actual results to differ materially from our expectations. If we receive an adverse judgment in any litigation, we could be required to pay substantial damages and cease certain practices or activities, including the manufacture, use and sale of products. With or without merit, litigation can be complex, can extend for a protracted period of time, can be very expensive and the expense can be unpredictable. Litigation initiated by us could also result in counter-claims against us, which could increase the costs associated with the litigation and result in our payment of damages or other judgments against us. In addition, litigation, and any related publicity, may divert the efforts and attention of some of our key personnel. Litigation may also harm the market prices of our securities.

We may be obligated to indemnify our current or former directors or employees, or former directors or employees of companies that we have acquired, in connection with litigation or regulatory investigations. These liabilities could be substantial and may include, among other things: the costs of defending lawsuits against these individuals; the cost of defending shareholder derivative suits; the cost of governmental, law enforcement or regulatory investigations; civil or criminal fines and penalties; legal and other expenses; and expenses associated with the remedial measures, if any, which may be imposed.

We are subject to laws, rules, and regulations in the U.S. and other countries relating to the collection, use, sharing, and security of third-party data including personal data, and our failure to comply with these laws, rules and regulations could subject us to proceedings by governmental entities or others and cause us to incur penalties, significant legal liability, or loss of customers, loss of revenue, and reputational harm .

We are subject to laws, rules, and regulations in the U.S. and other countries relating to the collection, use, and security of third-party data including data that relates to or identifies an individual person. In many cases, these laws apply not only to third-party transactions, but also to transfers of information between us and our subsidiaries, and among us, our subsidiaries and other parties with which we have commercial relations. Our possession and use of third-party data, including personal data and employee data in conducting our business subjects us to legal and regulatory burdens that may require us to notify vendors, customers or employees or other parties with which we have commercial relations of a data security breach and to respond to regulatory inquiries and to enforcement proceedings. Global privacy and data protection legislation, enforcement, and policy activity in this area are rapidly expanding and evolving, and may be inconsistent from jurisdiction to jurisdiction. Compliance requirements and even our inadvertent failure to comply with applicable laws may cause us to incur substantial costs, subject us to proceedings by governmental entities or others, and cause us to incur penalties or other significant legal liability, or lead us to change our business practices.

The nature of our industry and its reliance on IP and other proprietary information subjects us and our suppliers, customers and partners to the risk of significant litigation.

The data storage industry has been characterized by significant litigation. This includes litigation relating to patent and other IP rights, product liability claims and other types of litigation. We have historically been involved in frequent disputes regarding patent and other IP rights, and we have in the past received, and we may in the future receive, communications from third parties asserting that certain of our products, processes or technologies infringe upon their patent rights, copyrights, trademark rights or other IP rights. We may also receive claims of potential infringement if we attempt to license IP to others. IP risks increase when we enter into new markets where we have little or no IP protection as a defense against litigation. The complexity of the technology involved and the uncertainty of IP litigation increase the IP risks we face. Litigation can be expensive, lengthy and disruptive to normal business operations. Moreover, the results of litigation are inherently uncertain and may result in adverse rulings or decisions. We may be subject to injunctions, enter into settlements or be subject to judgments that may, individually or in the aggregate, have a material adverse effect on our business, financial condition or operating results.

If we incorporate third-party technology into our products or if claims or actions are asserted against us for alleged infringement of the IP of others, we may be required to obtain a license or cross-license, modify our existing technology or design a new non-infringing technology. Such licenses or design modifications can be extremely costly. We evaluate notices of alleged patent infringement and notices of patents from patent holders that we receive from time to time. We may decide to settle a claim or action against us, which settlement could be costly. We may also be liable for any past infringement. If there is an adverse ruling against us in an infringement lawsuit, an injunction could be issued barring production or sale of any infringing product. It could also result in a damage award equal to a reasonable royalty or lost profits or, if there is a finding of willful infringement, treble damages. Any of these results would increase our costs and harm our operating results. In addition, our suppliers, customers and partners are subject to similar risks of litigation, and a material, adverse ruling against a supplier, customer or partner could negatively impact our business.

Moreover, from time to time, we agree to indemnify certain of our suppliers and customers for alleged IP infringement. The scope of such indemnity varies but may include indemnification for direct and consequential damages and expenses, including attorneys' fees. We may be engaged in litigation as a result of these indemnification obligations. Third party claims for patent infringement are excluded from coverage under our insurance policies. A future obligation to indemnify our customers or suppliers may harm our business, financial condition and operating results.

Our reliance on IP and other proprietary information subjects us to the risk that these key ingredients of our business could be copied by competitors.

Our success depends, in significant part, on the proprietary nature of our technology, including non-patentable IP such as our process technology. We primarily rely on patent, copyright, trademark and trade secret laws, as well as nondisclosure agreements and other methods, to protect our proprietary technologies and processes. There can be no assurance that our existing patents will continue to be held valid, if challenged, or that they will have sufficient scope or strength to protect us. It is also possible that competitors or other unauthorized third parties may obtain, copy, use or disclose, illegally or otherwise, our proprietary technologies and processes, despite our efforts to protect our proprietary technologies and processes. If a competitor is able to reproduce or otherwise capitalize on our technology despite the safeguards we have in place, it may be difficult, expensive or impossible for us to obtain necessary legal protection. There are entities whom we believe may infringe our IP. Enforcement of our rights often requires litigation. If we bring a patent infringement action and are not successful, our competitors would be able to use similar technology to compete with us. Moreover, the defendant in such an action may successfully countersue us for infringement of their patents or assert a counterclaim that our patents are invalid or unenforceable. Also, the laws of some foreign countries may not protect our IP to the same extent as do U.S. laws. In addition to patent protection of IP rights, we consider elements of our product designs and processes to be proprietary and confidential. We rely upon employee, consultant and vendor non-disclosure agreements and contractual provisions and a system of internal safeguards to protect our proprietary information. However, any of our registered or unregistered IP rights may be challenged or exploited by others in the industry, which could harm our operating results.

The success of our branded products depends in part on the positive image that consumers have of our brands. We believe the popularity of our brands makes them a target of counterfeiting or imitation, with third parties attempting to pass off counterfeit products as our products. Any occurrence of counterfeiting, imitation or confusion with our brands could adversely affect our reputation and impair the value of our brands, which in turn could negatively impact sales of our branded products, our share and our gross margin, as well as increase our administrative costs related to brand protection and counterfeit detection and prosecution.

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The costs of compliance with state, federal and international legal and regulatory requirements, such as environmental, labor, trade, health, safety, anti-corruption and tax regulations, customers' standards of corporate citizenship, and industry and coalition standards, such as those established by the Electronics Industry Citizenship Coalition, could cause an increase in our operating costs.

We are subject to, and may become subject to additional, state, federal and international laws and regulations governing our environmental, labor, trade, health, safety, anti-corruption and tax practices. These laws and regulations, particularly those applicable to our international operations, are or may be complex, extensive and subject to change. We will need to ensure that we and our suppliers and partners timely comply with such laws and regulations, which may result in an increase in our operating costs. Legislation has been, and may in the future be, enacted in locations where we manufacture or sell our products. In addition, climate change and financial reform legislation is a significant topic of discussion and has generated and may continue to generate federal, international or other regulatory responses in the near future. If we or our suppliers or partners fail to timely comply with applicable legislation, our customers may refuse to purchase our products or we may face increased operating costs as a result of taxes, fines or penalties, or legal liability and reputational damage, which would have a materially adverse effect on our business, operating results and financial condition.

In connection with our compliance with environmental laws and regulations, as well as our compliance with industry and coalition environmental initiatives, such as those established by the Electronics Industry Citizenship Coalition, the standards of business conduct required by some of our customers, and our commitment to sound corporate citizenship in all aspects of our business, we could incur substantial compliance and operating costs and be subject to disruptions to our operations and logistics. In addition, if we were found to be in violation of these laws or noncompliant with these initiatives or standards of conduct, we could be subject to governmental fines, liability to our customers and damage to our reputation and corporate brand which could cause our financial condition and operating results to suffer.

Conflict minerals regulations may cause us to incur additional expenses and could limit the supply and increase the cost of certain components and metals contained in our products.

We are subject to the SEC's diligence and disclosure requirements regarding the use and source of gold, tantalum, tin and tungsten, commonly referred to as 3TG or conflict minerals, which are necessary to the functionality or production of products manufactured or contracted to be manufactured by public companies. These rules require us to determine and report annually whether such 3TG originated from the Democratic Republic of the Congo or an adjoining country. These rules could affect our ability to source components that contain 3TG, or 3TG generally, at acceptable prices and could impact the availability of such components or 3TG, since there may be only a limited number of suppliers of "conflict free" 3TG. Our customers, including our OEM customers, may require, and some of our customers have notified us that they require, that our products contain only conflict free 3TG, and our revenues and margins may be harmed if we are unable to meet this requirement at a reasonable price, or at all, or are unable to pass through any increased costs associated with meeting this requirement. Additionally, we may suffer reputational harm with our customers and other stakeholders and challenges from government regulators if our products are not conflict free or if we are unable to sufficiently verify the origins of the 3TG contained in our products through the due diligence procedures that we implement. We could incur significant costs to the extent that we are required to make changes to products, processes, or sources of supply due to the foregoing requirements or pressures. Conflict minerals legislation in Europe, Canada or any other jurisdiction, could increase these risks.

Violation of applicable laws, including labor or environmental laws, and certain other practices by our suppliers, customers or partners could harm our business.

We expect our suppliers, customers and partners to operate in compliance with applicable laws and regulations, including labor and environmental laws, and to otherwise meet our required standards of conduct. While our internal operating guidelines promote ethical business practices, we do not control our suppliers, customers, partners or their labor or environmental practices. The violation of labor, environmental or other laws by any of them, or divergence of their business practices from those generally accepted as ethical, could harm our business by:

- interrupting or otherwise disrupting the shipment of our product components;
- damaging our reputation;

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- forcing us to find alternate component sources;
- reducing demand for our products (for example, through a consumer boycott); or
- exposing us to potential liability for our suppliers', customers' or partners' wrongdoings.

Flash Ventures' equipment lease agreements contain covenants and other cancellation events, and cancellation of the leases would harm our business, operating results and financial condition.

Flash Ventures sells and leases back from a consortium of financial institutions ("lessors") a portion of its equipment and Flash Ventures has entered into equipment lease agreements, of which we and Toshiba each guarantee half of the total outstanding obligations. As of December 30, 2016, the portion of outstanding Flash Ventures' lease obligations covered by our guarantees totaled approximately \$1.1 billion, based upon the Japanese yen to U.S. dollar exchange rate at December 30, 2016. The equipment lease agreements contain covenants and cancellation events that are customary for Japanese lease facilities and that relate to Flash Ventures and each of the guarantors. Cancellation events relating to the guarantors include, among other things, an assignment of all or a substantial part of a guarantor's business, a bankruptcy event involving a guarantor and acceleration of other monetary debts of a guarantor above a specified threshold.

The breach of a covenant or the occurrence of another cancellation event could result in an acceleration of the Flash Ventures' lease obligations. If a cancellation event were to occur, Flash Ventures would be required to negotiate a resolution with the lessors, as well as other parties to the lease transactions, to avoid cancellation and acceleration of the lease obligations. Such resolution could include, among other things, supplementary security to be supplied by us, as guarantor, increased interest rates or waiver fees. If a cancellation event occurs and we fail to reach a resolution, we may be required to pay all or a portion of the outstanding lease obligations covered by our guarantees, which would significantly reduce our cash position and may force us to seek additional financing, which may not be available on terms acceptable to us, if at all.

Any decisions to reduce or discontinue paying cash dividends to our shareholders could cause the market price for our common stock to decline.

We may modify, suspend or cancel our cash dividend policy in any manner and at any time. Any reduction or discontinuance by us of the payment of quarterly cash dividends could cause the market price of our common stock to decline. Moreover, in the event our payment of quarterly cash dividends are reduced or discontinued, our failure or inability to resume paying cash dividends at historical levels could cause the market price of our common stock to decline.

Fluctuations in currency exchange rates as a result of our international operations may negatively affect our operating results.

Because we manufacture and sell our products abroad, our revenue, cost of goods sold, margins, operating costs and cash flows are impacted by fluctuations in foreign currency exchange rates. If the U.S. dollar exhibits sustained weakness against most foreign currencies, the U.S. dollar equivalents of unhedged manufacturing costs could increase because a significant portion of our production costs are foreign-currency denominated. Conversely, there would not be an offsetting impact to revenues since revenues are substantially U.S. dollar denominated. Additionally, we negotiate and procure some of our component requirements in U.S. dollars from non-U.S. based vendors. If the U.S. dollar weakens against other foreign currencies, some of our component suppliers may increase the price they charge for their components in order to maintain an equivalent profit margin. In addition, our purchases of NAND flash memory from Flash Ventures and our investment in Flash Ventures are denominated in Japanese yen. If the Japanese yen appreciates against the U.S. dollar, our cost of purchasing NAND flash wafers and the cost to us of future funding of Flash Ventures would increase, and the value of our investments denominated in Japanese yen would be higher, increasing our exposure to asset impairment. If any of these events occur, they would have a negative impact on our operating results.

Prices for our products are substantially U.S. dollar denominated, even when sold to customers that are located outside the U.S. Therefore, as a substantial portion of our sales are from countries outside the U.S., fluctuations in currency exchanges rates, most notably the strengthening of the U.S. dollar against other foreign currencies, contribute to variations in sales of products in impacted jurisdictions and could adversely impact demand and revenue growth. In addition, currency variations can adversely affect margins on sales of our products in countries outside the U.S.

We attempt to manage the impact of foreign currency exchange rate changes by, among other things, entering into short-term, foreign exchange contracts. However, these contracts do not cover our full exposure, and can be canceled by the counterparty if currency controls are put in place. Thus, our decisions and hedging strategy with respect to currency risks may not be successful and harm our operating results. Further, the ability to enter into foreign exchange contracts with financial institutions is based upon our available credit from such institutions and compliance with covenants and other restrictions. Operating losses, third party downgrades of our credit rating or instability in the worldwide financial markets could impact our ability to effectively manage our foreign currency exchange rate risk. Hedging also exposes us to the credit risk of our counterparty financial institutions.

Increases in our customers' credit risk could result in credit losses and term extensions under existing contracts with customers with credit losses could result in an increase in our operating costs.

Some of our OEM customers have adopted a subcontractor model that requires us to contract directly with companies, such as ODMs, that provide manufacturing and fulfillment services to our OEM customers. Because these subcontractors are generally not as well capitalized as our direct OEM customers, this subcontractor model exposes us to increased credit risks. Our agreements with our OEM customers may not permit us to increase our product prices to alleviate this increased credit risk. Additionally, as we attempt to expand our OEM and distribution channel sales into emerging economies such as Brazil, Russia, India and China, the customers with the most success in these regions may have relatively short operating histories, making it more difficult for us to accurately assess the associated credit risks. Any credit losses we may suffer as a result of these increased risks, or as a result of credit losses from any significant customer, especially in situations where there are term extensions under existing contracts with such customers, would increase our operating costs, which may negatively impact our operating results.

Our operating results fluctuate, sometimes significantly, from period to period due to many factors, which may result in a significant decline in our stock price.

Our quarterly operating results may be subject to significant fluctuations as a result of a number of other factors including:

- weakness in demand for one or more product categories;
- the timing of orders from and shipment of products to major customers, loss of major customers;
- our product mix;
- reductions in the ASPs of our products and lower margins;
- excess output, capacity or inventory, resulting in lower ASPs, financial charges or impairments, or insufficient output, capacity or inventory, resulting in lost revenue opportunities;
- inability to successfully transition to 3D NAND or other technology developments, or other failure to reduce product costs to keep pace with reduction in ASPs;
- manufacturing delays or interruptions;
- delays in design wins or customer qualifications, acceptance by customers of competing products in lieu of our products;
- success of our partnerships and joint ventures, in particular the volume, timing and cost of wafer production at Flash Ventures, and our success in managing the relationships with our strategic partners;
- inability to realize the potential benefits of our acquisitions and the success of our integration efforts;
- ability to penetrate new markets for our storage solutions;

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- variations in the cost of and lead times for components for our products, disruptions of our supply chain;
- limited availability of components that we obtain from a single or a limited number of suppliers;
- seasonal and other fluctuations in demand often due to technological advances;
- increase in costs due to warranty claims;
- higher costs as a result of currency exchange rate fluctuations; and
- availability and rates of transportation.

We often ship a high percentage of our total quarterly sales in the third month of the quarter, which makes it difficult for us to forecast our financial results before the end of the quarter. As a result of the above or other factors, our forecast of operating results for the quarter may differ materially from our actual financial results. If our results of operations fail to meet the expectations of analysts or investors, it could cause an immediate and significant decline in our stock price.

We have made and continue to make a number of estimates and assumptions relating to our consolidated financial reporting, and actual results may differ significantly from our estimates and assumptions.

We have made and continue to make a number of estimates and assumptions relating to our consolidated financial reporting. The highly technical nature of our products and the rapidly changing market conditions with which we deal means that actual results may differ significantly from our estimates and assumptions. These changes have impacted our financial results in the past and may continue to do so in the future. Key estimates and assumptions for us include:

- price protection adjustments and other sales promotions and allowances on products sold to retailers, resellers and distributors;
- inventory adjustments for write-down of inventories to lower of cost or market value (net realizable value);
- valuation of acquired assets, particularly intangibles, and liabilities assumed;
- testing of goodwill and other long-lived assets for impairment;
- reserves for doubtful accounts;
- accruals for product returns;
- accruals for warranty costs related to product defects;
- accruals for litigation and other contingencies;
- liabilities for unrecognized tax benefits; and
- expensing of stock-based compensation.

In addition, changes in existing accounting or taxation rules or practices, new accounting pronouncements or taxation rules, or varying interpretations of current accounting pronouncements or taxation practice could have an adverse effect on our results of operations and financial condition.

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The market price of our common stock is volatile.

The market price of our common stock has been, and may continue to be, volatile. Factors that may significantly affect the market price of our common stock include the following:

- actual or anticipated fluctuations in our operating results, including those resulting from the seasonality of our business;
- announcements of technological innovations by us or our competitors, which may decrease the volume and profitability of sales of our existing products and increase the risk of inventory obsolescence;
- new products introduced by us or our competitors;
- strategic actions by us or competitors, such as acquisitions and restructurings;
- periods of severe pricing pressures due to oversupply or price erosion resulting from competitive pressures or industry consolidation;
- developments with respect to patents or proprietary rights, and any litigation;
- proposed or adopted regulatory changes or developments or anticipated or pending investigations, proceedings or litigation that involve or affect us or our competitors;
- conditions and trends in the hard drive, solid state storage, flash memory, computer, mobile, data and content management, storage and communication industries;
- contraction in our operating results or growth rates that are lower than our previous high growth-rate periods;
- failure to meet analysts' revenue or earnings estimates or changes in financial estimates or publication of research reports and recommendations by financial analysts relating specifically to us or the storage industry in general;
- announcements relating to dividends and share repurchases; and
- macroeconomic conditions that affect the market generally and, in particular, developments related to market conditions for our industry.

In addition, the stock market is subject to fluctuations in the stock prices and trading volumes that affect the market prices of the stock of public companies, including us. These broad market fluctuations have adversely affected and may continue to adversely affect the market price of shares of our common stock. For example, expectations concerning general economic conditions may cause the stock market to experience extreme price and volume fluctuations from time to time that particularly affect the stock prices of many high technology companies. These fluctuations may be unrelated to the operating performance of the companies.

Securities class action lawsuits are often brought against companies after periods of volatility in the market price of their securities. A number of such suits have been filed against us in the past, and should any new lawsuits be filed, such matters could result in substantial costs and a diversion of resources and management's attention.

The resale of shares of common stock issued to Hitachi in connection with our acquisition of HGST could adversely affect the market price of our common stock.

On March 8, 2012, as partial consideration for our acquisition of HGST, we issued 25 million shares of our common stock to Hitachi. On each of November 6, 2013 and November 13, 2014, Hitachi completed a secondary offering of 12.5 million and 6.25 million, respectively, of these shares. Future sales of the remaining 6.25 million shares of our common stock held by Hitachi could adversely affect the market price of our common stock.

Our cash balances and investment portfolio are subject to various risks, any of which could adversely impact our financial position.

Given the international footprint of our business, we have both domestic and international cash balances and investments. We maintain an investment portfolio of various holdings, security types, and maturities. These investments are subject to general credit, liquidity, market, political, sovereign and interest rate risks, which may be exacerbated by unusual events that affect global financial markets. A material part of our investment portfolio consists of U.S. government securities and bank deposits. If global credit and equity markets experience prolonged periods of decline, or if there is a downgrade of the U.S. government credit rating due to an actual or threatened default on government debt, our investment portfolio may be adversely impacted and we could determine that our investments may experience an other-than-temporary decline in fair value, requiring impairment charges that could adversely affect our financial results. A failure of any of these financial institutions in which deposits exceed FDIC limits could also have an adverse impact on our financial position.

In addition, if we are unable to generate sufficient cash flows from operations to repay our indebtedness, fund acquisitions, pay dividends, or repurchase shares of our common stock, we may choose or be required to increase our borrowings, if available, or to repatriate funds to the U.S. at a substantial tax cost. We must comply with regulations regarding the conversion and distribution of funds earned in the local currencies of various countries. If we cannot comply with these or other applicable regulations, we may face increased difficulties in using cash generated in these countries.

If our internal controls are found to be ineffective, our stock price may be adversely affected.

Our most recent evaluation resulted in our conclusion that as of July 1, 2016, in compliance with Section 404 of the Sarbanes-Oxley Act of 2002, our internal control over financial reporting was effective. If our internal control over financial reporting is found to be ineffective or if we identify a material weakness in our financial reporting in future periods, investors may lose confidence in the reliability of our financial statements, we may be required to restate our financial results, our access to capital markets may be limited, and we may be subject to sanctions from regulatory agencies and The NASDAQ Global Select Market, each of which may adversely affect our stock price.

From time to time we may become subject to income tax examinations or similar proceedings, and as a result we may incur additional costs and expenses or owe additional taxes, interest and penalties that may negatively impact our operating results.

We are subject to income taxes in the U.S. and certain foreign jurisdictions, and our determination of our tax liability is subject to review by applicable domestic and foreign tax authorities. For example, as we have previously disclosed, we are under examination by the Internal Revenue Service for certain fiscal years and in connection with that examination, we received a Revenue Agent's Report seeking certain adjustments to income as disclosed in Part I, Item 1, Note 10 of the Notes to Condensed Consolidated Financial Statements included in this Quarterly Report on Form 10-Q. Although we believe our tax positions are properly supported, the final timing and resolution of any tax examinations are subject to significant uncertainty and could result in our having to pay amounts to the applicable tax authority in order to resolve examination of our tax positions, which could result in an increase or decrease of our current estimate of unrecognized tax benefits and may negatively impact our financial position, results of operations or cash flows.

We are subject to risks associated with loss or non-renewal of favorable tax treatment under agreements or treaties with foreign tax authorities.

Portions of our operations are subject to a reduced tax rate or are free of tax under various tax holidays that expire in whole or in part from time to time, or may be terminated if certain conditions are not met. Although many of these holidays may be extended when certain conditions are met, we may not be able to meet such conditions. If the tax holidays are not extended, or if we fail to satisfy the conditions of the reduced tax rate, then our effective tax rate could increase in the future. In addition, any actions by us to repatriate non-U.S. earnings for which we have not previously provided for U.S. taxes may impact our effective tax rate.

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Changes in tax laws could increase our worldwide tax rate and materially affect our financial position and results of operations.

Tax laws are dynamic and subject to change as new laws and regulations are passed and new interpretations of the laws are issued or applied. While the former U.S. administration and members of Congress made public statements indicating that tax reform is a priority, and certain changes to the U.S. tax laws and regulations have been proposed, additional changes may be proposed or implemented by the new U.S. President and his administration. In addition, many countries in the European Union, as well as a number of other countries and organizations such as the Organization for Economic Cooperation and Development, are actively considering changes to existing tax laws that, if enacted, could increase our tax obligations in many countries where we do business. Due to the large scale of our U.S. and international business activities, many of these proposed changes to the taxation of our activities, if enacted, could increase our worldwide effective tax rate and harm our financial position and results of operations.

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

None.

Item 3. *Defaults Upon Senior Securities*

None.

Item 4. *Mine Safety Disclosures*

Not applicable.

Item 5. *Other Information*

On February 2, 2017, our Board of Directors approved Amended and Restated By-laws (the “Amended By-laws”). In addition to purely ministerial or minor conforming changes, the Amended By-laws amend Section 1.02 thereof to change the location of our principal office to 5601 Great Oaks Parkway, City of San Jose, County of Santa Clara, State of California.

Item 6. *Exhibits*

The exhibits listed in the Exhibit Index (following the signature page of the Quarterly Report on Form 10-Q) are filed with, or incorporated by reference in, this Quarterly Report on Form 10-Q, as specified in the Exhibit List, from exhibits previously filed with the Securities and Exchange Commission. Certain agreements listed in the Exhibit Index that we have filed or incorporated by reference may contain representations and warranties by us or our subsidiaries. These representations and warranties have been made solely for the benefit of the other party or parties to such agreements and (i) may have been qualified by disclosures made to such other party or parties, (ii) were made only as of the date of such agreements or such other date(s) as may be specified in such agreements and are subject to more recent developments, which may not be fully reflected in our public disclosures, (iii) may reflect the allocation of risk among the parties to such agreements and (iv) may apply materiality standards different from what may be viewed as material to investors. Accordingly, these representations and warranties may not describe the actual state of affairs at the date hereof and should not be relied upon.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this Quarterly Report on Form 10-Q to be signed on its behalf by the undersigned, thereunto duly authorized.

WESTERN DIGITAL CORPORATION

By: /s/ MARK P. LONG

Mark P. Long

President WD Capital, Chief Strategy Officer and Chief Financial Officer

(Principal Financial Officer and Principal Accounting Officer)

Dated: February 7, 2017

EXHIBIT INDEX

Exhibit Number	Description
2.1	Agreement and Plan of Merger, dated as of October 21, 2015, among Western Digital Corporation, Schrader Acquisition Corporation and SanDisk Corporation (Filed as Exhibit 2.1 to the Company's Current Report on Form 8-K (File No. 1-08703) with the Securities and Exchange Commission on October 26, 2015)±
3.1	Amended and Restated Certificate of Incorporation of Western Digital Corporation, as amended to date (Filed as Exhibit 3.1 to the Company's Quarterly Report on Form 10-Q (File No. 1-08703) with the Securities and Exchange Commission on February 8, 2006)
3.2	Amended and Restated By-Laws of Western Digital Corporation, as amended effective as of February 2, 2017†
10.1	Western Digital Corporation Amended and Restated 2004 Performance Incentive Plan Non-Employee Director Restricted Stock Unit Grant Program, as amended November 4, 2016†*
10.2	Western Digital Corporation Summary of Compensation Arrangements for Named Executive Officers and Directors†*
10.3	Western Digital Corporation Executive Severance Plan, amended and restated as of February 2, 2017†*
12.1	Statement of Computation of Ratio of Earnings to Fixed Charges†
31.1	Certification of Principal Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002†
31.2	Certification of Principal Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002†
32.1	Certification of Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002**
32.2	Certification of Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002**
101.INS	XBRL Instance Document†
101.SCH	XBRL Taxonomy Extension Schema Document†
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document†
101.LAB	XBRL Taxonomy Extension Label Linkbase Document†
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document†
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document†

† Filed with this report.

* Management contract or compensatory plan or arrangement required to be filed as an exhibit pursuant to applicable rules of the Securities and Exchange Commission.

** Furnished with this report.

± Certain schedules have been omitted pursuant to Item 601(b)(2) of Regulation S-K. The Company agrees to furnish supplemental copies of any of the omitted schedules upon request by the Securities and Exchange Commission.

WESTERN DIGITAL CORPORATION
(a Delaware corporation)

AMENDED AND RESTATED BY-LAWS

(As Adopted on February 2, 2017)

ARTICLE I
Offices

1.01 Registered Office. The registered office of Western Digital Corporation (this “Corporation”) in the State of Delaware shall be at 2711 Centerville Road, Suite 400, Wilmington, County of New Castle, and the name of the registered agent in charge thereof shall be Corporation Service Company.

1.02 Principal Office . The principal office for the transaction of the business of this Corporation shall be 5601 Great Oaks Parkway, City of San Jose, County of Santa Clara, State of California. The Board of Directors (the “Board”) is hereby granted full power and authority to change said principal office from one location to another.

1.03 Other Offices. This Corporation may also have such other offices at such other places, either within or without the State of Delaware, as the Board may from time to time determine or as the business of this Corporation may require.

ARTICLE II
Meetings Of Stockholders

2.01 Annual Meetings . If required by applicable law, annual meetings of the stockholders of this Corporation shall be held for the purpose of electing directors and for the transaction of such proper business as may come before such meetings.

2.02 Special Meetings . Special meetings of the stockholders may be called at any time by the Board, the Chairman of the Board or the President.

2.03 Place of Meetings . All meetings of the stockholders shall be held at such time, date and place, if any, within or without the State of Delaware, as shall be designated from time to time by the Board and stated in the notice of the meeting or in a duly executed waiver of notice thereof. This Corporation may postpone, reschedule or cancel any meeting of stockholders previously scheduled by the Board.

2.04 Notice of Meetings . Whenever stockholders are required or permitted to take any action at a meeting, a notice of the meeting shall be given that shall state the place, if any, the date and time of the meeting, the means of remote communication, if any, by which stockholders and proxy holders may be deemed to be present in person and vote at such meeting, and, in the case of a special meeting, the purpose or purposes for which the meeting is called. Unless otherwise provided by law, the Certificate of Incorporation or these By-laws, the notice of any meeting shall be given not less than ten (10) nor more than sixty (60) days before the date of the

meeting to each stockholder entitled to vote at such meeting. If mailed, such notice shall be deemed to be given when deposited in the United States mail, postage prepaid, directed to the stockholder at such stockholder's address as it appears on the records of this Corporation. Notice to stockholders hereunder may be given by a form of electronic transmission in accordance with applicable law if consented to by the stockholders to whom the notice is given.

2.05 Adjournments. Any meeting of stockholders, annual or special, may be adjourned from time to time for any reason, whether or not a quorum is present, to reconvene at the same or some other place, if any, by either (i) the chairman of the meeting or (ii) a majority in voting power of the stockholders present in person or by proxy and entitled to vote thereon. Notice need not be given of any such adjourned meeting if the time and place, if any, or means of remote communication, if any, by which stockholders and proxy holders may be deemed to be present in person and vote at such adjourned meeting are announced at the meeting at which the adjournment is taken. At the adjourned meeting at which a quorum shall be present or represented, this Corporation may transact any business which might have been transacted at the original meeting. If the adjournment is for more than thirty (30) days, or if after the adjournment a new record date is fixed for the adjourned meeting, notice of the adjourned meeting shall be given to each stockholder of record entitled to vote at the meeting.

2.06 Quorum . Except as otherwise provided by law, the Certificate of Incorporation or these By-laws, at each meeting of stockholders the presence in person or by proxy of the holders of a majority in voting power of the outstanding shares of stock entitled to vote at the meeting shall be necessary and sufficient to constitute a quorum for the transaction of business thereat. In the absence of a quorum, then either (i) the chairman of the meeting or (ii) a majority in voting power of the stockholders present in person or by proxy and entitled to vote thereon, shall have power to adjourn the meeting from time to time in the manner provided in Section 2.05 of these By-laws until a quorum shall be present or represented.

2.07 Voting .

(a) Except as otherwise provided by or pursuant to the provisions of the Certificate of Incorporation, each stockholder entitled to vote at any meeting of stockholders shall be entitled to one vote for each share of stock held by such stockholder which has voting power upon the matter in question and which shall have been held by and registered in the name of the stockholder on the books of this Corporation on the date fixed pursuant to Section 2.10 of these By-laws as the record date for the determination of stockholders entitled to notice of and to vote at a meeting.

(b) Shares of its own stock belonging to this Corporation or to another corporation, if a majority of the shares entitled to vote in the election of directors of such other corporation is held, directly or indirectly, by this Corporation, shall neither be entitled to vote nor be counted for quorum purposes. Persons holding stock of this Corporation in a fiduciary capacity shall be entitled to vote such stock. Persons whose stock is pledged shall be entitled to vote, unless in the transfer by the pledgor on the books of this Corporation the pledgor shall have expressly empowered the pledgee to vote thereon. Stock having voting power that is held of record in the names of two or more persons, whether fiduciaries, members of a partnership, joint tenants in common, tenants by entirety or otherwise, or with respect to which two or more persons have the

same fiduciary relationship, shall be voted in accordance with the provisions of the General Corporation Law of the State of Delaware (the “General Corporation Law”).

(c) Any such voting rights may be exercised by the stockholder entitled thereto in person or by the stockholder’s proxy; provided, however, that no proxy shall be voted or acted upon after three years from its date unless said proxy shall provide for a longer period. A proxy shall be irrevocable if it states that it is irrevocable and if, and only as long as, it is coupled with an interest sufficient in law to support an irrevocable power. The attendance at any meeting of a stockholder who may theretofore have given a proxy which is not irrevocable shall not have the effect of revoking the same, unless the stockholder shall attend the meeting and vote in person or deliver to the Secretary prior to the voting of the proxy a revocation of the proxy or a new proxy bearing a later date. At any meeting of the stockholders at which a quorum is present all matters, except as otherwise provided in the Certificate of Incorporation, these By-laws, the rules or regulations of any stock exchange applicable to this Corporation, or applicable law or pursuant to any regulation applicable to this Corporation or its securities, shall be decided by the vote of a majority in voting power of the stockholders present in person or by proxy and entitled to vote thereon. The vote at any meeting of the stockholders on any question need not be by written ballot, unless so directed by the chairman of the meeting. On a vote by ballot each ballot shall be signed by the stockholder voting, or by his or her proxy, if there be such proxy, and it shall state the number of shares voted.

2.08 List of Stockholders . The officer who has charge of the stock ledger shall prepare and make, at least ten (10) days before every meeting of stockholders, a complete list of the stockholders entitled to vote at the meeting, arranged in alphabetical order, and showing the address of each stockholder and the number of shares registered in the name of each stockholder. Such list shall be open to the examination of any stockholder, for any purpose germane to the meeting at least ten (10) days prior to the meeting (a) on a reasonably accessible electronic network, provided that the information required to gain access to such list is provided with the notice of meeting or (b) during ordinary business hours at the principal place of business of this Corporation. The list of stockholders must also be open to examination at the meeting as required by applicable law. Except as otherwise provided by law, the stock ledger shall be the only evidence as to who are the stockholders entitled to examine the list of stockholders required by this Section 2.08 or to vote in person or by proxy at any meeting of stockholders.

2.09 Inspector of Elections . This Corporation shall, in advance of any meeting of stockholders, appoint one or more inspectors of election, who may be employees of this Corporation, to act at the meeting or any adjournment thereof and to make a written report thereof. This Corporation may designate one or more persons as alternate inspectors to replace any inspector who fails to act. In the event that no inspector is so appointed or designated or any inspector so appointed or designated is unable to act at a meeting of stockholders, the person presiding at the meeting shall appoint one or more inspectors to act at the meeting. Each inspector, before entering upon the discharge of his or her duties, shall take and sign an oath to execute faithfully the duties of inspector with strict impartiality and according to the best of his or her ability. The inspector or inspectors so appointed or designated shall (i) ascertain the number of shares of capital stock of this Corporation outstanding and the voting power of each such share, (ii) determine the shares of capital stock of this Corporation represented at the meeting and the validity of proxies and ballots, (iii) count all votes and ballots, (iv) determine

and retain for a reasonable period a record of the disposition of any challenges made to any determination by the inspectors, and (v) certify their determination of the number of shares of capital stock of this Corporation represented at the meeting and such inspectors' count of all votes and ballots. Such certification and report shall specify such other information as may be required by law. In determining the validity and counting of proxies and ballots cast at any meeting of stockholders of this Corporation, the inspectors may consider such information as is permitted by applicable law. No person who is a candidate for an office at an election may serve as an inspector at such election.

2.10 Fixing Date for Determination of Stockholder of Record . In order that this Corporation may determine the stockholders entitled to notice of or to vote at any meeting of stockholders or any adjournment thereof or entitled to receive payment of any dividend or other distribution or allotment of any rights, or entitled to exercise any rights in respect of any other change, conversion or exchange of stock or for the purpose of any other lawful action, the Board may fix a record date, which record date shall not precede the date upon which the resolution fixing the record date is adopted by the Board, and which record date: (1) in the case of determination of stockholders entitled to vote at any meeting of stockholders or adjournment thereof, shall, unless otherwise required by law, not be more than sixty (60) nor less than ten (10) days before the date of such meeting; and (2) in the case of any other action, shall not be more than sixty (60) days prior to such other action. If no record date is fixed: (1) the record date for determining stockholders entitled to notice of or to vote at a meeting of stockholders shall be at the close of business on the day next preceding the day on which notice is given, or, if notice is waived, at the close of business on the day next preceding the day on which the meeting is held; and (2) the record date for determining stockholders for any other purpose shall be at the close of business on the day on which the Board adopts the resolution relating thereto. A determination of stockholders entitled to notice of or to vote at a meeting of stockholders shall apply to any adjournment of the meeting; provided, however, that the Board may fix a new record date for the adjourned meeting.

2.11 Stockholder Proposals and Nominations.

(a) Annual Meetings of Stockholders.

(i) Nominations of persons for election to the Board and the proposal of business to be considered by the stockholders may be made at an annual meeting of stockholders only (A) pursuant to this Corporation's notice of meeting (or any supplement thereto), (B) by or at the direction of the Board or (C) by any stockholder of this Corporation who was a stockholder of record of this Corporation at the time the notice provided for in this Section 2.11 is delivered to the Secretary of this Corporation, who is entitled to vote at the meeting and who complies with the notice procedures set forth in this Section 2.11.

(ii) For nominations or other business to be properly brought before an annual meeting by a stockholder pursuant to clause (C) of paragraph (a)(i) of this Section 2.11, the stockholder must have given timely notice thereof in writing to the Secretary of this Corporation and any such proposed business other than the nominations of persons for election to the Board must constitute a proper matter for stockholder action. To be timely, a stockholder's notice shall be delivered to the Secretary at the principal executive offices of this Corporation not later than

the close of business on the ninetieth day nor earlier than the close of business on the one hundred twentieth day prior to the first anniversary of the preceding year's annual meeting (provided, however, that in the event that the date of the annual meeting is more than thirty (30) days before or more than seventy (70) days after such anniversary date, notice by the stockholder must be so delivered not earlier than the close of business on the one hundred twentieth day prior to such annual meeting and not later than the close of business on the later of the ninetieth day prior to such annual meeting or the tenth day following the day on which public announcement of the date of such meeting is first made by this Corporation). In no event shall the public announcement of an adjournment or postponement of an annual meeting commence a new time period (or extend any time period) for the giving of a stockholder's notice as described above. Such stockholder's notice shall set forth: (A) as to each person whom the stockholder proposes to nominate for election as a director (1) all information relating to such person that is required to be disclosed in solicitations of proxies for election of directors in an election contest, or is otherwise required, in each case pursuant to and in accordance with Section 14(a) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), and the rules and regulations promulgated thereunder, (2) such person's written consent to being named in the proxy statement as a nominee and to serving as a director if elected, and (3) include a completed and signed questionnaire, representation and agreement required by Section 2.11(c) of these By-laws; (B) as to any other business that the stockholder proposes to bring before the meeting, a brief description of the business desired to be brought before the meeting, the text of the proposal or business (including the text of any resolutions proposed for consideration and in the event that such business includes a proposal to amend the By-laws, the language of the proposed amendment), the reasons for conducting such business at the meeting and any material interest in such business of such stockholder and the beneficial owner, if any, on whose behalf the proposal is made; and (C) as to the stockholder giving the notice and the beneficial owner, if any, on whose behalf the nomination or proposal is made (1) the name and address of such stockholder, as they appear on this Corporation's books, and of such beneficial owner, (2) the class or series and number of shares of capital stock of this Corporation which are owned beneficially and of record by such stockholder and such beneficial owner as of the date of the notice, and a representation that the stockholder will notify this Corporation in writing within five (5) business days after the record date for such meeting of the class or series and number of shares of capital stock of this Corporation owned of record by the stockholder and such beneficial owner as of the record date for the meeting, (3) a description of any agreement, arrangement or understanding, including without limitation any agreements that would be required to be disclosed pursuant to Item 5 or Item 6 of Exchange Act Schedule 13D (regardless of whether the requirement to file a Schedule 13D is applicable to the stockholder or beneficial owner), with respect to the nomination or proposal between or among such stockholder and/or such beneficial owner, any of their respective affiliates or associates, and any others acting in concert with any of the foregoing (including, in the case of a nomination, the nominee), and a representation that the stockholder will notify this Corporation in writing within five (5) business days after the record date for such meeting of any such agreement, arrangement or understanding in effect as of the record date for the meeting, (4) a description of any agreement, arrangement or understanding (including any derivative or short positions, profit interests, options, warrants, convertible securities, stock appreciation or similar rights, hedging transactions, and borrowed or loaned shares) involving such stockholder or beneficial owner that is in effect as of the date of the stockholder's notice, whether or not such instrument or right shall be subject to settlement in underlying shares of

capital stock of this Corporation, the effect or intent of which is to mitigate loss to, manage risk or benefit from share price changes for, or increase or decrease the voting power of, such stockholder or such beneficial owner, with respect to securities of this Corporation, or which provides, directly or indirectly, the opportunity to profit or share in any profit derived from any decrease in the price or value of the shares of capital stock of this Corporation, and the class or series and number of shares of this Corporation's capital stock that relate to such agreements, arrangements or understandings and a representation that the stockholder will notify this Corporation in writing within five (5) business days after the record date for such meeting of any such agreement, arrangement or understanding of this nature in effect as of the record date for the meeting, (5) a description of any proxy (other than a revocable proxy or consent given in response to a solicitation made pursuant to, and in accordance with, Section 14(a) of the Exchange Act by way of a solicitation statement filed on Schedule 14A), agreement, arrangement, understanding or relationship in effect as of the date of the notice pursuant to which such stockholder or such beneficial owner has or shares a right to vote or direct any third party to vote any shares of capital stock of this Corporation and a representation that the stockholder will notify this Corporation in writing within five (5) business days after the record date for such meeting of any proxy, agreement, arrangement, understanding or relationship of this nature in effect as of the record date for the meeting, (6) a representation that the stockholder is a holder of record of stock of this Corporation entitled to vote at such meeting and intends to appear in person or by proxy at the meeting to propose such business or nomination, (7) a representation whether the stockholder or the beneficial owner, if any, intends or is part of a group which intends (x) to deliver a proxy statement and/or form of proxy to holders of at least the percentage of this Corporation's outstanding capital stock required to approve or adopt the proposal or elect the nominee and/or (y) otherwise to solicit proxies or votes from stockholders in support of such proposal or nomination, and (8) any other information relating to such stockholder and beneficial owner, if any, required to be disclosed in a proxy statement or other filings required to be made in connection with solicitations of proxies for, as applicable, the proposal and/or for the election of directors in an election contest pursuant to and in accordance with Section 14(a) of the Exchange Act and the rules and regulations promulgated thereunder. The foregoing notice requirements of this paragraph (a)(ii) of this Section 2.11 shall be deemed satisfied by a stockholder with respect to business other than a nomination if the stockholder has notified this Corporation of his or her intention to present a proposal at an annual meeting in compliance with applicable rules and regulations promulgated under the Exchange Act and such stockholder's proposal has been included in a proxy statement that has been prepared by this Corporation to solicit proxies for such annual meeting. This Corporation may require any proposed nominee to furnish such other information as it may reasonably require to determine the eligibility of such proposed nominee to serve as a director of this Corporation.

(iii) Notwithstanding anything in the second sentence of paragraph (a)(ii) of this Section 2.11 to the contrary, in the event that the number of directors to be elected to the Board at an annual meeting is increased effective after the time period for which nominations would otherwise be due under paragraph (a)(ii) of this Section 2.11 and there is no public announcement by this Corporation naming the nominees for the additional directorships at least one hundred (100) days prior to the first anniversary of the preceding year's annual meeting, a stockholder's notice required by this Section 2.11 shall also be considered timely, but only with respect to nominees for the additional directorships, if it shall be delivered to the Secretary at the

principal executive offices of this Corporation not later than the close of business on the tenth day following the day on which such public announcement is first made by this Corporation.

(b) Special Meetings of Stockholders. Only such business shall be conducted at a special meeting of stockholders as shall have been brought before the meeting pursuant to this Corporation's notice of meeting. Nominations of persons for election to the Board may be made at a special meeting of stockholders at which directors are to be elected pursuant to this Corporation's notice of meeting (i) by or at the direction of the Board or (ii) provided that the Board has determined that directors shall be elected at such meeting, by any stockholder of this Corporation who is a stockholder of record at the time the notice provided for in this Section 2.11 is delivered to the Secretary of this Corporation, who is entitled to vote at the meeting upon such election and who complies with the notice procedures set forth in this Section 2.11. In the event this Corporation calls a special meeting of stockholders for the purpose of electing one or more directors to the Board, any such stockholder entitled to vote in such election of directors may nominate a person or persons (as the case may be) for election to such position(s) as specified in this Corporation's notice of meeting, if the stockholder's notice required by paragraph (a)(ii) of this Section 2.11 shall be delivered to the Secretary at the principal executive offices of this Corporation not earlier than the close of business on the one hundred twentieth day prior to such special meeting and not later than the close of business on the later of the ninetieth day prior to such special meeting or the tenth day following the day on which public announcement is first made of the date of the special meeting and of the nominees proposed by the Board to be elected at such meeting. In no event shall the public announcement of an adjournment or postponement of a special meeting commence a new time period (or extend any time period) for the giving of a stockholder's notice as described above.

(c) Submission of Questionnaire, Representation and Agreement. To be eligible to be a nominee for election or reelection as a director of this Corporation, the candidate for nomination must have previously delivered (in accordance with the time periods prescribed for delivery of notice under this Section 2.11), to the Secretary at the principal executive offices of this Corporation, (i) a completed written questionnaire (in a form provided by this Corporation) with respect to the background, qualifications, stock ownership and independence of such proposed nominee and (ii) a written representation and agreement (in a form provided by this Corporation) that such candidate for nomination (A) is not and, if elected as a director during his or her term of office, will not become a party to (1) any agreement, arrangement or understanding with, and has not given and will not give any commitment or assurance to, any person or entity as to how such proposed nominee, if elected as a director of this Corporation, will act or vote on any issue or question (a "Voting Commitment") that has not been disclosed to the Corporation or (2) any Voting Commitment that could limit or interfere with such proposed nominee's ability to comply, if elected as a director of this Corporation, with such proposed nominee's fiduciary duties under applicable law, (B) is not, and will not become a party to, any agreement, arrangement or understanding with any person or entity other than this Corporation with respect to any direct or indirect compensation or reimbursement for service as a director that has not been disclosed therein and (C) if elected as a director of this Corporation, will comply with all applicable corporate governance, conflict of interest, confidentiality, stock ownership and trading and other policies and guidelines of this Corporation applicable to directors and in effect during such person's term in office as a director (and, if requested by any

candidate for nomination, the Secretary of this Corporation shall provide to such candidate for nomination all such policies and guidelines then in effect).

(d) General.

(i) Except as otherwise expressly provided in any applicable rule or regulation promulgated under the Exchange Act, only such persons who are nominated in accordance with the procedures set forth in this Section 2.11 shall be eligible to be elected at an annual or special meeting of stockholders of this Corporation to serve as directors and only such business shall be conducted at a meeting of stockholders as shall have been brought before the meeting in accordance with the procedures set forth in this Section 2.11. Except as otherwise provided by law, the chairman of the meeting shall have the power and duty (A) to determine whether a nomination or any business proposed to be brought before the meeting was made or proposed, as the case may be, in accordance with the procedures set forth in this Section 2.11 (including whether the stockholder or beneficial owner, if any, on whose behalf the nomination or proposal is made solicited (or is part of a group which solicited) or did not so solicit, as the case may be, proxies or votes in support of such stockholder's nominee or proposal in compliance with such stockholder's representation as required by clause (a)(ii)(C)(7) of this Section 2.11) and (B) if any proposed nomination or business was not made or proposed in compliance with this Section 2.11, to declare that such nomination shall be disregarded or that such proposed business shall not be transacted. Notwithstanding the foregoing provisions of this Section 2.11, unless otherwise required by law, if the stockholder does not provide the information with respect to which such stockholder represented under clause (a)(ii)(C) of this Section 2.11 it would notify this Corporation in writing within five (5) business days after the record date for the meeting of stockholders or if the stockholder (or a qualified representative of the stockholder) does not appear at the annual or special meeting of stockholders of this Corporation to present a nomination or proposed business, such nomination shall be disregarded and such proposed business shall not be transacted, notwithstanding that proxies in respect of such vote may have been received by this Corporation. For purposes of this Section 2.11, to be considered a qualified representative of the stockholder, a person must be a duly authorized officer, manager or partner of such stockholder or must be authorized by a writing executed by such stockholder or an electronic transmission delivered by such stockholder to act for such stockholder as proxy at the meeting of stockholders and such person must produce such writing or electronic transmission, or a reliable reproduction of the writing or electronic transmission, at the meeting of stockholders prior to the making of such nomination or proposal at such meeting.

(ii) For purposes of this Section 2.11, "public announcement" shall include disclosure in a press release reported by the Dow Jones News Service, Associated Press or comparable national news service or in a document publicly filed by this Corporation with the Securities and Exchange Commission pursuant to Section 13, 14 or 15(d) of the Exchange Act and the rules and regulations promulgated thereunder.

(iii) Notwithstanding the foregoing provisions of this Section 2.11, a stockholder shall also comply with all applicable requirements of the Exchange Act and the rules and regulations thereunder with respect to the matters set forth in this Section 2.11; provided however, that any references in these By-laws to the Exchange Act or the rules and regulations promulgated thereunder are not intended to and shall not limit any requirements applicable to

nominations or proposals as to any other business to be considered pursuant to this Section 2.11 (including paragraphs (a)(i)(C) and (b) hereof), and compliance with paragraphs (a)(i)(C) and (b) of this Section 2.11 shall be the exclusive means for a stockholder to make nominations or submit other business (other than, as provided in the penultimate sentence of (a)(ii), business other than nominations brought properly under and in compliance with Rule 14a-8 of the Exchange Act, as may be amended from time to time). Nothing in this Section 2.11 shall be deemed to affect any rights (A) of stockholders to request inclusion of proposals or nominations in this Corporation's proxy statement pursuant to applicable rules and regulations promulgated under the Exchange Act or (B) of the holders of any series of Preferred Stock to elect directors pursuant to any applicable provisions of the Certificate of Incorporation.

2.12 Conduct of Meetings. The date and time of the opening and the closing of the polls for each matter upon which the stockholders will vote at a meeting shall be announced at the meeting by the person presiding over the meeting. The Board may adopt by resolution such rules and regulations for the conduct of the meeting of stockholders as it shall deem appropriate. Except to the extent inconsistent with such rules and regulations as adopted by the Board, the person presiding over any meeting of stockholders shall have the right and authority to postpone, convene and (for any reason or no reason) to recess and/or adjourn the meeting, to prescribe such rules, regulations and procedures and to do all such acts as, in the judgment of such presiding person, are appropriate for the proper conduct of the meeting. Such rules, regulations or procedures, whether adopted by the Board or prescribed by the presiding person over the meeting, may include, without limitation, the following: (a) the establishment of an agenda or order of business for the meeting; (b) rules and procedures for maintaining order at the meeting and the safety of those present (including, without limitation, rules and procedures for removal of disruptive persons from the meeting); (c) limitations on attendance at or participation in the meeting to stockholders entitled to vote at the meeting, their duly authorized and constituted proxies or such other persons as the presiding person of the meeting shall, in his or her discretion, determine; (d) restrictions on entry to the meeting after the time fixed for the commencement thereof; and (e) limitations on the time allotted to questions or comments by participants. The presiding person at any meeting of stockholders, in addition to making any other determinations that may be appropriate to the conduct of the meeting (including, without limitation, determinations with respect to the administration and/or interpretation of any of the rules, regulations or procedures of the meeting, whether adopted by the Board or prescribed by the person presiding over the meeting), shall, if the facts warrant, determine and declare to the meeting that a matter or business was not properly brought before the meeting and if such presiding person should so determine, such presiding person shall so declare to the meeting and any such matter or business not properly brought before the meeting shall not be transacted or considered. Unless and to the extent determined by the Board or the person presiding over the meeting, meetings of stockholders shall not be required to be held in accordance with the rules of parliamentary procedure.

2.13 Organization . Meetings of stockholders shall be presided over by the Chairman of the Board, or in his or her absence by the Vice Chairman, if any, or in his or her absence, by the Chief Executive Officer or, in his or her absence, by a person designated by the Board, or in the absence of such designation by a person chosen by a majority vote of the stockholders present in person or represented by proxy at the meeting. The Secretary shall act as secretary of

the meeting, but in his or her absence the person presiding over the meeting may appoint any person to act as secretary of the meeting.

ARTICLE III Board of Directors

3.01 General Powers . Subject to the requirements of the General Corporation Law, the property, business and affairs of this Corporation shall be managed by the Board.

3.02 Number and Term of Office . The Board shall consist of one or more members, the number thereof to be determined from time to time by resolution of the Board. Directors need not be stockholders. Each of the directors of this Corporation shall hold office until his or her successor shall have been duly elected and shall qualify or until he or she shall resign or shall have been removed in the manner provided in these By-laws.

3.03 Election of Directors .

(a) The directors shall be elected annually by the stockholders of this Corporation. Except as otherwise provided in Section 3.05 below, each director shall be elected by the vote of a majority of the votes cast with respect to such director's election at any annual or special meeting for the election of directors at which a quorum is present. If, however, as of the tenth (10th) day preceding the date the notice of the meeting is first mailed for such meeting to the stockholders of this Corporation, the number of nominees exceeds the number of directors to be elected (a "Contested Election"), the nominees receiving the greatest number of votes of the shares represented in person or by proxy at the meeting and entitled to vote on the election of directors, up to the number of directors to be elected, shall be the directors. For purposes of this Section 3.03, a "majority of the votes cast" means that the number of shares voted "for" a nominee must exceed the number of votes cast "against" that nominee (with "abstentions" and "broker non-votes" not counted as a vote cast either "for" or "against" that director's election).

(b) If an incumbent director is not reelected but would otherwise remain in office until his or her successor is elected and qualified, the director shall offer to tender his or her resignation to the Board, which may be conditioned upon acceptance of such resignation by the Board. If a resignation is so conditioned, the Governance Committee of the Board, or such other committee designated by the Board pursuant to Section 3.15 below, will evaluate any such resignation in light of the best interests of this Corporation and its stockholders and will make a recommendation to the Board on whether to accept or reject such resignation or whether other action should be taken with respect thereto. In making its recommendation, such committee may consider any factors it deems relevant, including the director's qualifications, the director's past and expected future contributions to this Corporation, the overall composition of the Board and whether accepting the tendered resignation would cause this Corporation to fail to satisfy or otherwise comply with any applicable rule or regulation (including listing requirements of The NASDAQ Stock Market LLC and the federal securities laws). The Board will act on the resignation, taking into account the recommendation of such committee, and this Corporation will publicly disclose (by a press release and filing an appropriate disclosure with the Securities and Exchange Commission) the Board's decision regarding the resignation and, if such resignation is rejected, the rationale behind the decision within ninety (90) days from the date of

the certification of the election results. The director who tenders his or her resignation will not participate in the decision of the Board or Board committee.

(c) If the Board accepts a director's resignation pursuant to this By-law, or if a nominee for director is not elected and the nominee is not an incumbent director, then the Board may fill the resulting vacancy in accordance with the provisions of these By-laws or may decrease the size of the Board in accordance with the provisions of these By-laws.

(d) If no directors receive the requisite majority vote at an annual or special meeting held for the election of directors that is not a Contested Election, the incumbent Board will nominate a new slate of directors and hold a special meeting for the purpose of electing those nominees within one hundred eighty (180) days after the certification of the stockholder vote at the prior meeting. In this circumstance, the incumbent Board will continue to serve until new directors are duly elected and qualified.

3.04 Resignations . Any director of this Corporation may resign at any time by giving notice in writing or by electronic transmission to the Board or to the Secretary of this Corporation. Any such resignation shall take effect at the time specified therein, or, if the time be not specified, it shall take effect immediately upon its receipt by the Board or the Secretary; and unless otherwise specified therein, the acceptance of such resignation shall not be necessary to make it effective.

3.05 Vacancies . Except as otherwise provided in the Certificate of Incorporation, any vacancy in the Board, whether because of death, resignation, disqualification, an increase in the number of directors, or any other cause, may be filled by vote of the majority of the remaining directors, although less than a quorum, or by a plurality of the votes cast at a meeting of stockholders. Each director so chosen to fill a vacancy shall hold office until his or her successor shall have been elected and shall qualify or until he or she shall resign or shall have been removed in the manner provided in these By-laws. If there are no directors in office, then an election of directors may be held in the manner provided by the General Corporation Law.

3.06 Place of Meeting, Etc . The Board may hold any of its meetings at such place or places within or without the State of Delaware as the Board may from time to time by resolution designate or as shall be designated by the person or persons calling the meeting or in the notice or a waiver of notice of any such meeting. Directors may participate in any regular or special meeting of the Board by means of conference telephone or similar communications equipment pursuant to which all persons participating in the meeting of the Board can hear each other, and such participation shall constitute presence in person at such meeting.

3.07 Annual Meeting . The Board shall meet as soon as practicable after each annual election of directors and notice of such first meeting shall not be required, provided a quorum shall be present; or such meeting may be held at such time and place as shall be specified in a notice given as hereinafter provided for special meetings of the Board, or as shall be specified in a waiver given by each person entitled to notice.

3.08 Regular Meetings . Regular meetings of the Board shall be held at such times and places as the Board shall from time to time by resolution determine. If any day fixed for a

regular meeting shall be a legal holiday at the place where the meeting is to be held, then the meeting shall be held at the same time and place on the next succeeding business day not a legal holiday.

3.09 *Special Meetings* . Special meetings of the Board for any purpose or purposes may be called at any time by the Chairman of the Board, the Chief Executive Officer, the President, the Secretary or any two directors. Notice of a special meeting of the Board shall be given by the person or persons calling the meeting at least twenty-four (24) hours before the special meeting.

3.10 *Quorum and Manner of Acting* . Except as otherwise provided in these By-laws, the Certificate of Incorporation or by law, the presence of a majority of the authorized number of directors shall be required to constitute a quorum for the transaction of business at any meeting of the Board, and all matters shall be decided at any such meeting, a quorum being present, by the affirmative votes of a majority of the directors present. In the absence of a quorum, a majority of directors present at any meeting may adjourn the same from time to time until a quorum shall be present. Notice of any adjourned meeting need not be given. The directors shall act only as a Board, and the individual directors shall have no power as such.

3.11 *Action by Consent* . Any action required or permitted to be taken at any meeting of the Board or of any committee thereof may be taken without a meeting if all members of the Board or of such committee, as the case may be, consent thereto in writing or by electronic transmission, and such writing or writings or electronic transmissions are filed with the minutes of proceedings of the Board or committee.

3.12 *Removal of Directors* . Except as otherwise provided by the Certificate of Incorporation or applicable law, any director may be removed at any time, either with or without cause, by the affirmative vote of the stockholders then entitled to vote at an election of directors having a majority of the voting power of this Corporation given at an annual meeting or a special meeting of the stockholders called for such purpose.

3.13 *Compensation* . The directors shall receive only such compensation for their services as directors as may be allowed by resolution of the Board. The Board may also provide that this Corporation shall reimburse each such director for any expense incurred by such director on account of his or her attendance at any meetings of the Board or committees of the Board. Neither the payment of such compensation nor the reimbursement of such expenses shall be construed to preclude any director from serving this Corporation or its subsidiaries in any other capacity and receiving compensation therefor.

3.14 *Chairman and Vice Chairman of the Board of Directors* . This Corporation shall have a Chairman of the Board and, at its discretion, a Vice Chairman of the Board. Any such Chairman of the Board or Vice Chairman of the Board may be an officer of this Corporation if determined by the Board in its discretion. The Chairman of the Board, and in his or her absence the Vice Chairman of the Board, shall preside at all meetings of the stockholders and of the Board. The Chairman of the Board and the Vice Chairman of the Board shall have such other powers and duties as may from time to time be assigned to him or her by the Board or as may be prescribed by the By-laws.

3.15 Committees .

(a) The Board may appoint one or more committees, each consisting of one or more directors, and delegate to such committees any of the authority of the Board permitted by law except with respect to:

(i) the approval or adoption, or the making of a recommendation to the stockholders with respect to, any action or matter that is required under the General Corporation Law to be submitted to the stockholders;

(ii) the filling of vacancies on the Board or on any committee;

(iii) except as otherwise required by law or the rules and regulations of any nationally recognized securities exchange on which shares of this Corporation's stock are traded, the fixing of compensation of the directors for serving on the Board or on any committee;

(iv) the amendment or repeal of these By-laws or the adoption of new By-laws;

(v) the amendment or repeal of any resolution of the Board which by its express terms is not amendable or repealable;

(vi) distribution to the stockholders of this Corporation except at a rate or in a periodic amount or within a price range determined by the Board; or

(vii) the appointment of other committees of the Board or the members thereof.

(b) Any such committee must be appointed by resolution adopted by the Board and may be designated an Executive Committee or by such other name as the Board shall specify. The Board may designate one or more directors as alternate members of any committee, who may replace any absent member at any meeting of the committee. The Board shall have the power to prescribe the manner in which proceedings of any such committee shall be conducted. In the absence of any such prescription, such committee shall have the power to prescribe the manner in which its proceedings shall be conducted. Unless the Board or such committee shall provide, the regular and special meetings of any such committee shall be governed by the provisions of this Article applicable to meetings and actions of the Board. Minutes shall be kept of each meeting of such committee and filed with the Secretary of this Corporation.

3.16 Executive Committee . The passage of any resolution of the committee designated by the Board as the Executive Committee shall, in addition to any other limitations prescribed by the Board in accordance with the provisions of Section 3.15, require the affirmative vote of a majority of directors present and voting on such resolution who are not employees of this Corporation.

3.17 Rights of Inspection . Every director shall have the right to any reasonable time to inspect and copy all books, records, and documents of every kind and to inspect the physical properties of this Corporation and also of its subsidiaries, domestic or foreign. Such inspection

by a director may be made in person or by agent or attorney and includes the right to copy and obtain extracts.

3.18 Organization. Meetings of the Board shall be presided over by the Chairman of the Board, or in his or her absence by the Vice Chairman of the Board, if any, or in his or her absence by the Chief Executive Officer if such person is a member of the Board, or in his or her absence by a chairperson chosen at the meeting. The Secretary shall act as secretary of the meeting, but in his or her absence the chairperson of the meeting may appoint any person to act as secretary of the meeting.

ARTICLE IV Officers

4.01 Corporate Officers.

(a) The officers of this Corporation shall consist of a Chief Executive Officer, a President, a Secretary and a Chief Financial Officer. At the discretion of the Board, the Chairman of the Board may be an officer of this Corporation.

(b) In addition to the officers specified in Section 4.01(a), the Board may appoint such additional officers as the Board may deem necessary or desirable, including one or more Vice Presidents, one or more Assistant Secretaries, a Treasurer and one or more Assistant Treasurers, each of whom shall hold office for such period, have such authority and perform such duties as the Board may from time to time determine. The Board may delegate to any officer of this Corporation or any committee of the Board the power to appoint, remove and prescribe the term and duties of any officer provided for in this Section 4.01(b).

(c) One person may hold two or more offices, except that the Secretary may not hold the office of President.

4.02 Appointment and Term of Office. Each officer shall serve at the pleasure of the Board and shall hold office until a successor shall have been appointed or until such officer's death, disqualification, resignation or removal. Any officer may be removed, either with or without cause, by the Board or, except in case of an officer appointed by the Board, by any officer upon whom such power of removal may be conferred by the Board.

4.03 Resignations. Any officer may resign at any time by giving written notice of such officer's resignation to this Corporation. Any such resignation shall take effect at the time specified therein, or, if the time be not specified, upon receipt thereof by this Corporation. Unless otherwise specified therein, the acceptance of such resignation shall not be necessary to make it effective.

4.04 Vacancies. A vacancy in any office because of death, resignation, removal or disqualification or other event, may be filled in the manner prescribed in these By-laws for regular appointments to such office.

4.05 Chief Executive Officer. The Chief Executive Officer shall have, subject to the control of the Board, general and active supervision, direction and control of the business of this

Corporation and its officers, agents and employees, and shall perform all duties as may from time to time be assigned to him or her by the Board.

4.06 *President.* The President of this Corporation shall have the general powers and duties of management usually vested in the office of president and general manager of a corporation and shall have such other authority and shall perform such other duties as may from time to time be assigned to him or her by the Board or Chief Executive Officer.

4.07 *Secretary.* The Secretary shall keep or cause to be kept, at the principal executive office of this Corporation or at such other place as the Board may order, a book of minutes of all meetings of the stockholders, the Board and its committees, the time and place, if any, of holding such meetings, whether regular or special, and, if special, how authorized, the notice thereof given, the names of those present at Board and committee meetings, the number of shares present or represented at stockholder meetings and the proceedings thereof. The Secretary shall keep, or shall cause to be kept, at the principal executive office or at the office of this Corporation's transfer agent or registrar, a share register, or a duplicate share register, showing the names of stockholders and their addresses, the number and classes of shares of stock held by each, the number and date of certificates representing such shares and the number and date of cancellation of every certificate surrendered for cancellation. The Secretary shall give, or shall cause to be given, in conformity with these By-laws, notice of all meetings of the stockholders and of the Board and of any committees thereof requiring notice. The Secretary shall keep the seal of this Corporation in safe custody and shall have such other powers and shall perform such other duties as may from time to time be assigned to him or her by the Board.

4.08 *Chief Financial Officer.* The Chief Financial Officer shall keep and maintain, or shall cause to be kept and maintained, adequate and correct accounts of the properties and business transactions of this Corporation, and shall send or shall cause to be sent to the stockholders of this Corporation such financial statements and reports as are by law or by these By-laws required to be sent to them. The books of account shall at all reasonable times be open to inspection by any director. The Chief Financial Officer shall render to the Chief Executive Officer and directors, whenever they request it, an account of all transactions as Chief Financial Officer and of the financial condition of this Corporation, and shall have such other powers and perform such other duties as may from time to time be assigned to him or her by the Board.

4.09 *Compensation.* The compensation of those officers appointed by the Board pursuant to Section 4.01(a) or (b) of these By-laws shall be fixed from time to time by the Board or a committee of the Board delegated with such authority. No officer shall be prevented from receiving compensation by reason of the fact that such officer is also a director of this Corporation or any of its subsidiaries. Nothing contained herein shall preclude any officer from serving this Corporation or any of its subsidiaries, in any other capacity and receiving compensation therefor.

ARTICLE V

Contracts, Checks, Drafts, Bank Accounts, Etc.

5.01 *Execution of Contracts.* The Board, except as in these By-laws otherwise provided, may authorize any officer or officers, agent or agents, to enter into any contract or

execute any instrument in the name of and on behalf of this Corporation, and such authority may be general or confined to specific instances. Unless so authorized by the Board or by these By-laws, no officer, agent or employee shall have any power or authority to bind this Corporation by any contract or engagement or to pledge its credit or to render it liable for any purpose or in any amount.

5.02 *Checks, Drafts, Etc.* All checks, drafts or other orders for payment of money, notes or other evidence of indebtedness, issued in the name of or payable to this Corporation, shall be signed or endorsed by such person or persons and in such manner as, from time to time, shall be determined by resolution of the Board. Each authorized person shall give such bond, if any, as the Board may require.

5.03 *Deposits* . All funds of this Corporation not otherwise employed shall be deposited from time to time to the credit of this Corporation in such banks, trust companies and other depositories as the Board may select, or as may be selected by any officer or officers, assistant or assistants, agent or agents, or attorney or attorneys of this Corporation to whom such power shall have been delegated by the Board. For the purpose of deposit and for the purpose of collection for the account of this Corporation, the Chief Executive Officer, the President, the Chief Financial Officer and any Treasurer appointed in accordance with Section 4.01(b) (or any other officer or officers, assistant or assistants, agent or agents, or attorney or attorneys of this Corporation who shall from time to time be determined by the Board) may each endorse, assign and deliver checks, drafts and other orders for the payment of money which are payable to the order of this Corporation.

5.04 *General and Special Bank Accounts* . The Board may from time to time authorize the opening and keeping of general and special bank accounts with such banks, trust companies or other depositories as the Board may select or as may be selected by any officer or officers, assistant or assistants, agent or agents, or attorney or attorneys of this Corporation to whom such power shall have been delegated by the Board. The Board may make such special rules and regulations with respect to such bank accounts, not inconsistent with the provisions of these By-laws, as it may deem expedient.

ARTICLE VI

Shares and Their Transfer

6.01 *Certificates of Stock; Uncertificated Shares.*

(a) The shares of stock of this Corporation shall be represented by certificates, provided that the Board may provide by resolution or resolutions that some or all of any or all classes or series of its stock shall be uncertificated shares. Any such resolution shall not apply to shares represented by a certificate until such certificate is surrendered to this Corporation. Notwithstanding the adoption of any resolution providing for uncertificated shares, every holder of stock represented by certificates and upon request every holder of uncertificated shares shall be entitled to have a certificate, in such form as the Board shall prescribe, signed by, or in the name of this Corporation by the Chairman or Vice Chairman of the Board, or the President or Vice President, and by the Treasurer or an Assistant Treasurer, or the Secretary or an Assistant Secretary of this Corporation representing the number of shares registered in certificate form.

Any of or all of the signatures on the certificates may be by facsimile. In case any officer, transfer agent or registrar who has signed, or whose facsimile signature has been placed upon, any such certificate shall have ceased to be such officer, transfer agent or registrar before such certificate is issued, such certificate may nevertheless be issued by this Corporation with the same effect as though the person who signed such certificate, or whose facsimile signature shall have been placed thereupon, were such officer, transfer agent or registrar at the date of issue.

(b) A record shall be kept of the respective names of the persons, firms or corporations owning the stock represented by certificates or registered in uncertificated form, the number and class of shares represented by such certificates or registered in uncertificated form, and in case of cancellation, the respective dates of cancellation. Every certificate surrendered to this Corporation for exchange or transfer shall be cancelled, and, where the shares are to be represented by certificates, no new certificate or certificates shall be issued in exchange for any existing certificate until such existing certificate shall have been so cancelled, except in cases provided for in Section 6.04. Uncertificated shares shall be cancelled and issuance of new equivalent uncertificated shares shall be made to the person entitled thereto and the transaction shall be recorded upon the books of this Corporation.

6.02 Transfers of Stock . Shares of capital stock of this Corporation shall be transferable in the manner prescribed by law and in these By-laws. Shares of capital stock of this Corporation shall only be transferred on the books of this Corporation by the holder of record thereof or by such holder's attorney duly authorized in writing, upon surrender to this Corporation of the certificate or certificates representing such shares endorsed by the appropriate person or persons (or, with respect to uncertificated shares, by delivery of duly executed instructions or in any other manner permitted by applicable law), with such evidence of the authenticity of such endorsement or execution, transfer, authorization, and other matters as this Corporation may reasonably require, and accompanied by all necessary stock transfer stamps.

6.03 Regulations . Subject to the provisions of the Certificate of Incorporation and these By-laws, the Board may make such additional rules and regulations as it may deem expedient concerning the issue, transfer and registration of certificates representing shares of the stock of this Corporation or uncertificated shares.

6.04 Lost, Stolen, Destroyed, and Mutilated Certificates . In any case of loss, theft, destruction, or mutilation of any certificate of stock, another may be issued in its place upon proof of such loss, theft, destruction, or mutilation and upon the giving of a bond of indemnity to this Corporation in such form and in such sum as the Board may direct; provided, however, that a new certificate may be issued without requiring any bond when, in the judgment of the Board, it is proper to do so.

ARTICLE VII Indemnification

7.01 Scope of Indemnification . This Corporation shall indemnify and hold harmless, to the fullest extent permitted by applicable law as it presently exists or may hereafter be amended, any person (a "Covered Person") who was or is made or is threatened to be made a party or is otherwise involved in any action, suit or proceeding, whether civil, criminal,

administrative or investigative (a “proceeding”), by reason of the fact that he or she, or a person for whom he or she is the legal representative, is or was a director or officer of this Corporation or, while a director or officer of this Corporation, is or was serving at the request of this Corporation as a director, officer, member, manager, partner, employee or agent of another corporation or of a partnership, limited liability company, joint venture, trust, other enterprise or nonprofit entity, including service with respect to employee benefit plans, against all liability and loss suffered and expenses (including attorneys’ fees) actually and reasonably incurred by such Covered Person in connection with such proceeding. Notwithstanding the preceding sentence, except as otherwise provided in Section 7.06, this Corporation shall be required to indemnify a Covered Person pursuant to this Article VII in connection with a proceeding (or part thereof) commenced by such Covered Person only if the commencement of such proceeding (or part thereof) by the Covered Person was authorized in the specific case by the Board.

7.02 Advancement of Expenses . This Corporation shall to the fullest extent not prohibited by applicable law pay the expenses (including attorneys’ fees) incurred by a Covered Person in defending any proceeding in advance of its final disposition, provided, however, that, to the extent required by law, such payment of expenses in advance of the final disposition of the proceeding shall be made only upon receipt of an undertaking by the Covered Person to repay all amounts advanced if it should be ultimately determined that the Covered Person is not entitled to be indemnified under this Article VII or otherwise.

7.03 Other Rights and Remedies . The rights conferred on any Covered Person by this Article VII shall not be exclusive of any other rights which such Covered Person may have or hereafter acquire under any statute, provision of the Certificate of Incorporation, these By-laws, agreement, vote of stockholders or disinterested directors or otherwise.

7.04 Continuation of Indemnification and Advancement of Expenses . The indemnification and advancement of expenses provided by, or granted pursuant to, this Article VII shall, unless otherwise provided when authorized or ratified, continue as to a person who has ceased to be a director or officer and shall inure to the benefit of the heirs, executors and administrators of such a person.

7.05 Insurance . Upon resolution passed by the Board, this Corporation may purchase and maintain insurance on behalf of any person who is or was a director, officer, employee or agent of this Corporation or, while a director, officer, employee or agent of this Corporation, is or was serving at the request of this Corporation as a director, officer, member, manager, partner, employee or agent of another corporation, partnership, limited liability company, joint venture, trust or other enterprise against any liability asserted against such person and incurred by such person in any such capacity, or arising out of such person’s status as such, whether or not this Corporation would have the power to indemnify such person against such liability under the provisions of this Article.

7.06 Claims. If a claim for indemnification (following the final disposition of such action, suit or proceeding) under this Article VII is not paid in full within forty-five (45) days after a written claim therefor by the Covered Person has been received by this Corporation or if a claim for any advancement of expenses under this Article VII is not paid in full within thirty (30) days after this Corporation has received a statement or statements requesting such amounts to be

advanced, the Covered Person shall thereupon (but not before) be entitled to file suit to recover the unpaid amount of such claim and, if successful in whole or in part, shall be entitled to be paid the expense of prosecuting such claim to the fullest extent permitted by law. In any such action, this Corporation shall have the burden of proving that the Covered Person is not entitled to the requested indemnification or advancement of expenses under applicable law.

7.07 *Amendment or Repeal* . Any right to indemnification and advancement of expenses of any person covered by the provisions of this Article VII arising hereunder shall not be eliminated or impaired by an amendment to or repeal of these By-laws after the occurrence of the act or omission that is the subject of the proceeding for which indemnification or advancement of expenses is sought.

7.08 *Other Indemnification and Advancement of Expenses* . This Article VII shall not limit the right of this Corporation, to the extent and in the manner permitted by law, to indemnify and to advance expenses to persons other than Covered Persons when and as authorized by appropriate corporate action.

ARTICLE VIII Miscellaneous

8.01 *Fiscal Year*. The fiscal year of this Corporation shall be determined by resolution of the Board.

8.02 *Seal* . The Board shall adopt a corporate seal, which shall be in the form of a circle and shall bear the name of this Corporation and words and figures showing that this Corporation was incorporated in the State of Delaware and the year of incorporation.

8.03 *Manner of Notice; Waiver of Notices* . Except as otherwise provided herein or permitted by applicable law, notices to directors and stockholders shall be in writing and delivered personally or mailed to the directors or stockholders at their addresses appearing on the books of this Corporation. Notice to directors may be given by telecopier, telephone or other means of electronic transmission. Any waiver of notice, given by the person entitled to notice, whether before or after the time stated therein, shall be deemed equivalent to notice. Attendance of a person at a meeting (whether in person or by proxy in the case of a meeting of stockholders) shall constitute a waiver of notice of such meeting, except when the person attends a meeting for the express purpose of objecting, at the beginning of the meeting, to the transaction of any business because the meeting is not lawfully called or convened. Neither the business to be transacted at nor the purpose of any regular or special meeting of the stockholders, directors, or members of a committee of directors need be specified in a waiver of notice.

8.04 *Form of Records*. Any records maintained by this Corporation in the regular course of its business, including its stock ledger, books of account, and minute books, may be kept on, or by means of, or be in the form of, any information storage device or method, provided that the records so kept can be converted into clearly legible paper form within a reasonable time.

8.05 *Amendments* . These By-laws, or any of them, may be altered, amended or repealed, and new By-laws may be adopted, (i) by the Board, by vote of a majority of the

number of directors then in office as directors, acting at any duly called and held meeting of the Board, or (ii) by the stockholders, provided that notice of such proposed amendment, modification, repeal or adoption is given in the notice of special meeting. To the extent permitted by law, any By-laws made or altered by the stockholders may be altered or repealed by either the Board or the stockholders.

8.06 Representation of Other Corporations . The President, any Vice President, or the Secretary of this Corporation are each authorized to vote, represent and exercise on behalf of this Corporation all rights incident to any and all shares of or other equity interests in any other corporation or entity standing in the name of this Corporation. The authority herein granted to said officers to vote or represent on behalf of this Corporation any and all shares or equity interests held by this Corporation in any other corporation or entity may be exercised either by such officers in person or by any person authorized so to do by proxy or power of attorney duly executed by said officers.

WESTERN DIGITAL CORPORATION
AMENDED AND RESTATED 2004 PERFORMANCE INCENTIVE PLAN
NON-EMPLOYEE DIRECTOR RESTRICTED STOCK UNIT GRANT PROGRAM

1. **Establishment**. The Corporation maintains the Western Digital Corporation Non-Employee Directors Restricted Stock Unit Program (the “**Program**”), which is hereby amended and restated in its entirety effective as of November 4, 2016 (the “**Effective Date**”). This amendment and restatement of the Program is effective as to grants on and after the Effective Date; awards granted under the Program prior to the Effective Date are governed by the applicable terms of the Program as in effect on the date of grant of the award. The Program has been restated as an Appendix to, and any shares of Common Stock issued with respect to awards granted under the Program on and after the Effective Date shall be charged against the applicable share limits of, the Western Digital Corporation Amended and Restated 2004 Performance Incentive Plan (the “**Plan**”). Except as otherwise expressly provided herein, the provisions of the Plan shall govern all awards made pursuant to the Program. Capitalized terms are defined in the Plan if not defined herein.
 2. **Purpose**. The purpose of the Program is to promote the success of the Corporation and the interests of its stockholders by providing members of the Board who are not officers or employees of the Corporation or one of its Subsidiaries (“**Non-Employee Directors**”) an opportunity to acquire an ownership interest in the Corporation and more closely aligning the interests of Non-Employee Directors and stockholders.
 3. **Participation**. An award of Stock Units (a “**Stock Unit Award**”) under the Program shall be made only to Non-Employee Directors, shall be evidenced by a Notice of Award of Stock Units substantially in the form attached as Exhibit 1 hereto and shall be further subject to such other terms and conditions set forth therein. As used in the Program, 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 Common Stock (subject to adjustment as provided in Section 7.1 of the Plan) solely for purposes of the Program. Stock Units shall be used solely as a device for the determination of the number of shares of Common Stock to eventually be delivered to a Non-Employee Director if Stock Units held by such Non-Employee Director vest pursuant to Section 6 or Section 8. Stock Units shall not be treated as property or as a trust fund of any kind. Stock Units granted to a Non-Employee Director pursuant to the Program shall be credited to an unfunded bookkeeping account maintained by the Corporation on behalf of the Non-Employee Director (a “**Program Account**”).
 4. **Annual Stock Unit Awards**.
 - 4.1 **Annual Awards**. On the date of and immediately following the Corporation’s regular annual meeting of stockholders in each year during the term of the Plan commencing with 2012, each Non-Employee Director then in office shall be granted automatically (without any action by the Board or the Administrator) a Stock Unit Award with respect to a number (rounded down to the nearest whole number) of Stock Units equal to (i) \$225,000 (\$275,000 in the case of a Non-Employee Director then serving as Chair of the Board and \$255,000 in the case of a Non-Employee Director then serving as Lead Independent Director), divided by (ii) the Fair Market Value of a share of Common Stock on the applicable annual meeting date (subject to adjustment as provided in Section 7.1 of the Plan). An individual who was previously a member of the Board, who then ceased to be a member of the Board for any reason, and who then again becomes a Non-Employee Director shall thereupon again become eligible to be granted Stock Units under this Section 4.1.
 - 4.2 **Initial Award for New Directors**. Upon first being appointed or elected to the Board, a Non-Employee Director who has not previously served on the Board shall be granted automatically (without any action by the Board or the Administrator) a Stock Unit Award with respect to a number of Stock Units equal to (i) the number of Stock Units in the Annual Award immediately preceding the date such Non-Employee Director is first appointed or elected to the Board, divided by (ii) 365, multiplied by (iii) the number of days from the date such Non-Employee Director is first appointed or elected to the Board to the scheduled date of the Corporation’s next annual meeting of stockholders.
 - 4.3 **Transfer Restrictions**. Stock Units granted pursuant to this Section 4 shall be subject to the transfer restrictions set forth in Section 5.7 of the Plan. For purposes of clarity, the Administrator has not approved any transfer exceptions with respect to Stock Units granted pursuant to the Program in accordance with Section 5.7.2 of the Plan.
 5. **Dividend and Voting Rights**.
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5.1 **Limitation of Rights Associated with Stock Units** . A Non-Employee Director shall have no rights as a stockholder of the Corporation, no dividend rights (except as expressly provided in Section 5.2 with respect to dividend equivalent rights) and no voting rights, with respect to Stock Units granted pursuant to the Program and any shares of Common Stock underlying or issuable in respect of such Stock Units until such shares of Common Stock are actually issued to and held of record by the Non-Employee Director. 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.

5.2 **Dividend Equivalent Rights** . As of any date that the Corporation pays a dividend (other than in shares of Common Stock) upon issued and outstanding Common Stock, or makes a distribution (other than in shares of Common Stock) with respect thereto, a Non-Employee Director's Program Account shall be credited with an additional number (rounded down to the nearest whole number) of Stock Units equal to (i) the "fair value" of any dividend (or other distribution) with respect to one share of Common Stock, multiplied by (ii) the number of unpaid Stock Units credited to the Non-Employee Director's Program Account immediately prior to such dividend or distribution, divided by (iii) the Fair Market Value of a share of Common Stock on the date of payment of such dividend or distribution. In the case of a cash dividend or distribution, the "fair value" thereof shall be the amount of such cash, and, in the case of any other dividend or distribution (other than in shares of Common Stock), the "fair value" thereof shall be such amount as shall be determined in good faith by the Administrator. Stock Units credited pursuant to the foregoing provisions of this Section 5.2 shall be subject to the same vesting, payment and other terms, conditions and restrictions as the original Stock Units to which they relate. No adjustment shall be made pursuant to Section 7.1 of the Plan as to Stock Units granted pursuant to the Program in connection with any dividend (other than in shares of Common Stock) or distribution (other than in shares of Common Stock) for which dividend equivalents are credited pursuant to the foregoing provisions of this Section 5.2. Stock Units granted pursuant to the Program shall otherwise be subject to adjustment pursuant to Section 7.1 of the Plan (for example, and without limitation, in connection with a split or reverse split of the outstanding Common Stock).

6. **Vesting** . Subject to Section 8 hereof and Section 7 of the Plan, a Stock Unit Award granted to a Non-Employee Director pursuant to the Program (whether pursuant to Section 4 or Section 5.2) shall vest and become payable as to 100% of the total number of Stock Units subject thereto on the first to occur of (i) the first anniversary of the date of grant of the Stock Unit Award or (ii) immediately prior to the Corporation's first regular meeting of stockholders following the date of grant of the Stock Unit Award.

7. **Continuation of Services** . The vesting schedule requires continued service through each applicable vesting date as a condition to the vesting of the applicable installment of a Stock Unit Award and the rights and benefits under the Program. Service for only a portion of the vesting period, even if a substantial portion, will not entitle a Non-Employee Director to any proportionate vesting or avoid or mitigate a termination of rights and benefits upon or following a termination of services as provided in Section 8 below. Nothing contained in the Program constitutes a continued service commitment by the Corporation, confers upon a Non-Employee Director any right to remain in service to the Corporation, interferes with the right of the Corporation at any time to terminate such service, or affects the right of the Corporation to increase or decrease a Non-Employee Director's other compensation.

8. **Termination of Directorship** . Subject to earlier termination pursuant to Section 7 of the Plan, if a Non-Employee Director incurs a Separation from Service (as defined below) for any reason, the following rules shall apply with respect to any Stock Units granted to the Non-Employee Director pursuant to Section 4 above:

- other than as expressly provided below in this Section 8, all Stock Units granted to the Non-Employee Director pursuant to the Program that have not vested as of the Non-Employee Director's Separation from Service, shall immediately terminate without payment therefor;
- if the Non-Employee Director's Separation from Service occurs due to his or her death or Disability (as defined below), all Stock Units granted to the Non-Employee Director pursuant to the Program shall immediately vest and become payable as provided in Section 9;
- if the Non-Employee Director ceases to be a member of the Board due to his or her Removal, all then-unvested Stock Units granted to the Non-Employee Director pursuant to the Program shall immediately terminate without payment therefor.

For purposes of this Section 8, the term "**Disability**" shall mean a period of disability during which a Non-Employee Director qualified for permanent disability benefits under the Corporation's long-term disability plan, or, if the Non-Employee Director does not participate in such a plan, a period of disability during which the Non-Employee Director would have

qualified for permanent disability benefits under such a plan had the Non-Employee Director been a participant in such a plan, as determined in the sole discretion of the Administrator. If the Corporation does not sponsor such a plan, or discontinues to sponsor such a plan, Disability shall be determined by the Administrator in its sole discretion. For purposes of this Section 8, the term “ **Removal** ” shall mean the removal of a Non-Employee Director from the Board, with or without cause, in accordance with the Corporation’s Certificate of Incorporation, Bylaws or the Delaware General Corporation Law.

For purposes of this Section 8, the term “ **Separation from Service** ,” with respect to a Non-Employee Director, shall mean the date the Non-Employee Director ceases to be a member of the Board (regardless of the reason); provided, however, that if the Non-Employee Director is immediately thereafter employed by the Corporation or one of its Subsidiaries, such director’s Separation from Service shall be the date such director incurs a “separation from service” as such term is defined for purposes of Section 409A of the Code.

9. **Timing and Manner of Payment of Stock Units** . Except as provided in Section 10 below, on or within fifteen (15) business days following the first to occur of (i) the first anniversary of the date of grant of the Stock Unit Award, or (ii) the Non-Employee Director’s Separation from Service, the Corporation shall deliver to the Non-Employee Director a number of shares of Common Stock (either by delivering one or more certificates for such shares or by entering such shares in book entry form, as determined by the Corporation in its sole discretion) equal to the number of Stock Units (if any) that vested with respect to the corresponding Stock Unit Award in accordance with the provisions hereof, subject to adjustment as provided in Section 7 of the Plan; provided, however, that, to the extent permitted by the Corporation’s Amended and Restated Deferred Compensation Plan, as it may be amended from time to time (the “ **Deferred Compensation Plan** ”), a Non-Employee Director may elect to defer receipt of any or all shares of Common Stock payable with respect to Stock Units that vest pursuant to the Program. Such elections shall be made, and any such deferral shall be effected and administered, in accordance with the Deferred Compensation Plan. The Corporation’s obligation to deliver shares of Common Stock with respect to vested Stock Units is subject to the condition precedent that the Non-Employee Director (or other person entitled under the Plan to receive any shares with respect to the vested Stock Units) deliver to the Corporation any representations or other documents or assurances required pursuant to Section 8.1 of the Plan. A Non-Employee Director shall have no further rights with respect to any Stock Units that are paid or that are terminated pursuant to Section 8 hereof or Section 7 of the Plan, and such Stock Units shall be removed from the Non-Employee Director’s Program Account upon the date of such payment or termination.

10. **Change in Control Events** . A Stock Unit Award may vest and become payable in connection with the occurrence of certain events involving the Corporation as provided for in Section 7 of the Plan; provided, however, that, notwithstanding anything to the contrary in the Program or the Plan, if the event giving rise to such accelerated vesting is not also a “change in the ownership or effective control” of the Corporation or a “change in the ownership of a substantial portion of the assets” of the Corporation for purposes of Section 409A of the Code or an acceleration of payment of the award would otherwise result in any tax liability pursuant to Section 409A of the Code, then payment with respect to such vested Stock Unit Award shall not be made until such Stock Unit Award would have become vested and payable without regard to this Section 10 or Section 7 of the Plan.

11. **Plan Provisions; Maximum Number of Shares; Amendment; Administration; Construction** . Stock Units granted under the Program shall otherwise be subject to the terms of the Plan (including, without limitation, the provisions of Section 7 of the Plan). If Stock Unit Awards otherwise required pursuant to the Program would otherwise exceed any applicable share limit under Section 4.2 of the Plan, such grants shall be made pro-rata to Non-Employee Directors entitled to such grants. The Board may from time to time amend the Program without stockholder approval; provided that no such amendment shall materially and adversely affect the rights of a Non-Employee Director as to a Stock Unit Award granted under the Program before the adoption of such amendment. The Board may amend, modify, suspend or terminate outstanding Stock Unit Awards; provided, however, that outstanding Stock Unit Awards shall not be amended, modified, suspended or terminated so as to impair any rights of the recipient of the award without the consent of such recipient. If any such amendment or modification to an outstanding Stock Unit Award has the result of accelerating the vesting of such award, then any election that had been made to defer receipt of payment with respect to any or all of the Stock Units subject to the award pursuant to the Deferred Compensation Plan shall be disregarded. The Program does not limit the Board’s authority to make other, discretionary award grants to Non-Employee Directors pursuant to the Plan. The Plan Administrator’s power and authority to construe and interpret the Plan and awards thereunder pursuant to Section 3.1 of the Plan shall extend to the Program and awards granted hereunder. As provided in Section 3.2 of the Plan, any action taken by, or inaction of, the Administrator relating or pursuant to the Program and within its authority or under applicable law shall be within the absolute discretion of that entity or body and shall be conclusive and binding upon all persons. It is intended that the terms of the Program and all Stock Unit Awards granted under the Program will not result in the imposition of any tax liability pursuant to Section 409A of the Code. The Program and all Stock Unit Awards granted hereunder shall be construed and interpreted consistent with that intent.

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Western Digital Corporation
 Summary of Compensation Arrangements
 for
 Named Executive Officers and Directors
 January 2017

NAMED EXECUTIVE OFFICERS

Base Salaries . The current annual base salaries for the executive officers of Western Digital Corporation (the “Company”) who were named in the Summary Compensation Table in the Company’s Proxy Statement that was filed with the Securities and Exchange Commission in connection with the Company’s 2016 Annual Meeting of Stockholders (the “Named Executive Officers”) are as follows:

Named Executive Officer	Title	Current Base Salary
Stephen D. Milligan	Chief Executive Officer	\$ 1,150,000
Michael D. Cordano	President and Chief Operating Officer	\$ 800,000
Mark P. Long	Executive Vice President, Finance and Chief Strategy Officer	\$ 625,000
Michael C. Ray	Executive Vice President,	\$ 550,000

Semi-Annual Bonuses . Under the Company’s Amended and Restated 2004 Performance Incentive Plan, the Named Executive Officers are also eligible to receive cash bonus awards pursuant to the short-term incentive program (“STI”) under the Company’s Incentive Compensation Plan. The cash bonus awards are determined based on the Company’s achievement of performance goals pre-established by the Compensation Committee (the “Committee”) of the Company’s Board of Directors (for fiscal 2016, pre-established adjusted earnings per share goals) as well as other factors.

Additional Compensation . The Named Executive Officers are also eligible to receive equity-based incentives as determined by the Committee, entitled to participate in various Company plans, and for Mr. Milligan, subject to an employment agreement, in each case as set forth in exhibits to the Company’s filings with the Securities and Exchange Commission. In addition, the Named Executive Officers may be eligible to receive perquisites and other personal benefits as disclosed in the Company’s Proxy Statement filed with the Securities and Exchange Commission in connection with the Company’s 2016 Annual Meeting of Stockholders.

DIRECTORS

Annual Retainer and Committee Retainer Fees . The following table sets forth the current annual retainer and committee membership fees payable to each of the Company’s non-employee directors:

Type of Fee	Current Annual Retainer Fees
Annual Retainer	\$ 75,000
Additional Non-Executive Chairman of Board Retainer	\$ 100,000
Additional Committee Retainers	
• Audit Committee	\$ 15,000
• Compensation Committee	\$ 12,500
• Governance Committee	\$ 7,500
Additional Committee Chairman Retainers	
• Audit Committee	\$ 25,000
• Compensation Committee	\$ 22,500
• Governance Committee	\$ 12,500

The annual retainer fees are paid immediately following the Annual Meeting of Stockholders. Non-employee directors do not receive a separate fee for each Board of Directors or committee meeting they attend. However, the Company reimburses all non-employee directors for reasonable out-of-pocket expenses incurred to attend each Board of Directors or committee meeting. Mr. Milligan, who is an employee of the Company, does not receive any compensation for his service on the Board or any Board committee.

Additional Director Compensation . The Company's non-employee directors are also entitled to participate in the following other Company plans as set forth in exhibits to the Company's filings with the Securities and Exchange Commission: Non-Employee Director Restricted Stock Unit Grant Program, as adopted under the Company's Amended and Restated 2004 Performance Incentive Plan; and Deferred Compensation Plan.

WESTERN DIGITAL CORPORATION
EXECUTIVE SEVERANCE PLAN

1. PURPOSE

The purpose of the Plan is to provide severance benefits to certain Executives whose employment with the Company or a Subsidiary terminates under certain circumstances as described more fully herein.

2. EFFECTIVE DATE

All of the policies and practices of the Company and its Subsidiaries regarding severance benefits or similar payments upon employment termination with respect to Executives designated to participate in the Plan, other than written employment, separation or equity award agreements with the Company or a Subsidiary that provide severance benefits or the Company's Amended and Restated Change of Control Severance Plan, are hereby superseded by the Plan, which shall be known as the Western Digital Corporation Executive Severance Plan, effective as of the Effective Date. The Plan was initially approved by the Board on February 16, 2006 and most recently amended and restated on February 2, 2017.

3. DEFINITIONS

"Administrator" means the Committee or any delegate of such committee acting within the authority delegated to it pursuant to Section 9.1.

"Base Pay" means the employee's wages earned on a monthly basis, determined as of the employment termination date, excluding bonuses and commissions.

"Board" means the Board of Directors of the Company.

"Cause" means the occurrence or existence of any of the following with respect to an Executive:

- (a) the Executive's conviction by, or entry of a plea of guilty or *nolo contendere* in, a court of competent jurisdiction for any crime involving moral turpitude or any felony punishable by imprisonment in the jurisdiction involved;
 - (b) whether prior or subsequent to the Effective Date, the Executive's willful engaging in dishonest or fraudulent actions or omissions;
 - (c) failure or refusal to perform his or her duties as reasonably required by the Company and/or a Subsidiary that employs the Executive;
 - (d) negligence, insubordination, violation by the Executive of any duty (of loyalty or otherwise) owed to the Company and/or a Subsidiary, or any other misconduct on the part of the Executive;
 - (e) repeated non-prescription use of any controlled substance, or the repeated use of alcohol or any other non-controlled substance which in the Administrator's (or its delegate's or delegates') reasonable determination interferes with the Executive's service as an officer or employee of the Company and/or a Subsidiary;
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- (f) sexual harassment by the Executive that has been reasonably substantiated and investigated;
- (g) involvement in activities representing conflicts of interest with the Company and/or a Subsidiary;
- (h) improper disclosure of confidential information;
- (i) conduct endangering, or likely to endanger, the health or safety of another employee;
- (j) falsifying or misrepresenting information on the records of the Company and/or a Subsidiary;
- (k) the Executive's physical destruction or theft of substantial property or assets of the Company and/or a Subsidiary; or
- (l) breach of any policy of, or agreement with, the Company and/or a Subsidiary applicable to the Executive or to which the Executive is otherwise bound.

Review of any determination that a termination is for Cause shall be by the Administrator, in its sole and exclusive judgment and discretion, in accordance with the provisions of Section 8 herein.

"Change in Control" has the meaning ascribed to such term in the Company's Amended and Restated Change of Control Severance Plan; provided, however, that a transaction shall not constitute a Change in Control unless it is a "change in the ownership or effective control" of the Company, or a change "in the ownership of a substantial portion of the assets" of the Company within the meaning of Section 409A of the Code.

"Code" means the United States Internal Revenue Code of 1986, as amended.

"Committee" means the Compensation Committee of the Board of Directors of the Company.

"Company" means Western Digital Corporation, a Delaware corporation.

"Effective Date" means February 16, 2006.

"Eligible Employee" means any person classified by the Company or a Subsidiary, in its sole discretion, as a non-temporary, full-time or part-time, salaried or hourly employee (specifically excluding any individual who is not classified by the Company or a Subsidiary as a common law employee, such as an independent contractor or an individual working through a third-party provider, such as Kelly Services, without regard to the characterization or recharacterization of such individual's status by any court or governmental agency), who is paid from the United States payroll of the Company or a Subsidiary (each such individual, a "U.S. Eligible Employee"), or who is paid from a payroll of the Company or a Subsidiary outside of the United States (each such individual, a "Non-U.S. Eligible Employee"); provided, however, that in no event shall any employee who is paid from the United States payroll of the Company or a Subsidiary who as of the Effective Date is a party to a written employment agreement with the Company or a Subsidiary (other than an agreement providing for at-will employment by the Company or a Subsidiary and for no specified term) be an Eligible Employee; provided, further, that, as to any employee whose compensation requires approval by the Committee pursuant to the Committee's charter

at the time of such employee's termination of employment, such employee will be considered a "U.S. Eligible Employee" and not a "Non-U.S. Eligible Employee" for purposes of this Plan.

"ERISA" means the Employee Retirement Income Security Act of 1974, as amended.

"Executive" means an Eligible Employee who has been designated by the Board or the Committee (with respect to U.S. Eligible Employees) or by the Administrator or its delegate (with respect to Non-U.S. Eligible Employees) as a Participant in the Plan. The Board or the Committee shall designate an Executive as a Tier I Executive, Tier II Executive or Tier III Executive for purposes of participation in the Plan.

"Participant" means an Executive who is entitled, based on the provisions hereof, to severance benefits under Section 6.

"Plan" means this Western Digital Corporation Executive Severance Plan, as set forth in this instrument as it may be amended from time to time.

"Separation from Service," with respect to an Executive, shall mean that the Executive dies, retires, or otherwise has a termination of employment with the Company that constitutes a "separation from service" within the meaning of Treasury Regulation Section 1.409A-1(h)(1), without regard to the optional alternative definitions available thereunder.

"Subsidiary" means any corporation or other entity a majority of whose outstanding voting stock or voting power is beneficially owned directly or indirectly by the Company.

4. TERM

The Plan's initial term commenced on the Effective Date and continued in effect through December 31, 2008; provided, however, that on each anniversary of December 31, 2008, the term of the Plan shall extend automatically for one additional year, unless the Committee (or the Board) causes the Company to deliver written notice prior to the end of such extended term to each Executive then covered by the Plan that the term of the Plan will not be further extended, and if such notice is timely given, the Plan shall terminate at the end of the term then in progress.

5. PARTICIPATION

Upon approval of the Plan, the Committee designated the Executives initially covered by the Plan. The Committee (or, with respect to Non-U.S. Eligible Employees, the Administrator or its delegate) may, from time to time, designate additional Eligible Employees as Executives for purposes of participation in the Plan; provided, that the Committee (or the Administrator or its delegate, as applicable) shall limit the group of all persons eligible to participate in the Plan to a "select group of management or highly compensated employees" within the meaning of 29 C.F.R. 2520-104-23 or any similar successor provision. The Committee (or, with respect to Non-U.S. Eligible Employees, the Administrator) may, in its sole discretion, remove an Executive from participation in the Plan, and the Committee from time to time may approve modifications to the Tier to which one or more Executives have been designated.

6. SEVERANCE BENEFITS

6.1 Severance Benefits to Executives. An Executive whose employment with the Company or a Subsidiary is terminated by the Company or such Subsidiary, as applicable, without Cause shall become, subject to the conditions set forth in Section 7, a Participant under the Plan and entitled to the benefits set

forth in this Section 6. The severance benefits provided under Sections 6.2, 6.3, 6.5 and 6.6 of the Plan shall be the obligations of, and shall be provided to the Executive by, the entity (the Company or a Subsidiary, as applicable) that employs the Executive immediately prior to the Executive's termination of employment. For avoidance of doubt, in no event shall an Executive become entitled to or receive any payment hereunder if the Executive's employment with the Company or a Subsidiary is terminated voluntarily by the Executive (for any reason), by the Company or a Subsidiary, as applicable, for Cause, or on account of the Executive's death or disability (as defined in Section 22(e)(3) of the Code). Notwithstanding anything else contained herein to the contrary, an Executive shall not be deemed to have terminated employment if his or her employment by the Company or a Subsidiary terminates but he or she continues as an employee of the Company or another Subsidiary. The payments set forth in Sections 6.2, 6.3 and 6.6 shall be paid to the Participant in a single lump sum cash payment, subject to applicable tax withholding, during the ten (10) day period commencing on the thirtieth (30th) day following the date on which the Participant's Separation from Service occurs (or, in the case of a group termination (as determined by the Administrator), during the ten (10) day period commencing on the sixtieth (60th) day following the date on which the Participant's Separation from Service occurs). The payment rules of this paragraph are subject to Section 6.7.

6.2 Cash Severance Payment. A Participant shall receive a severance payment equal to the Participant's monthly rate of Base Pay multiplied by the number of months set forth below:

- (a) Tier I Executive: 24 months
- (b) Tier II Executive: 18 months
- (c) Tier III Executive: 12 months

6.3 Bonus. A Participant shall receive a payment equal to a pro-rata portion of the Participant's bonus opportunity under the Company's (or a Subsidiary's) bonus program in which the Participant participates for the bonus cycle in which the Participant's date of termination occurs (with such pro-rata portion based on the number of days in the applicable bonus cycle during which the Participant was employed (not to exceed the number of days in such bonus cycle (e.g., six (6) months)) and assuming 100% of the performance target(s) subject to the bonus award are met regardless of actual funding by the Company or a Subsidiary).

6.4 Equity Awards. Notwithstanding anything in the applicable stock incentive plan and/or award agreement to the contrary, upon a Participant's termination of employment, the Participant's then outstanding Company stock options and restricted stock or stock unit awards (together, "equity awards") shall be treated as follows: (a) the Participant's equity awards that are subject to time-based vesting will vest and become exercisable or payable, as applicable, as if the Participant had remained employed with the Company or a Subsidiary for an additional six (6) months; and (b) the Participant's equity awards that were granted with performance-based vesting requirements that, as of such termination of the Participant's employment, have (in whole or in part) been credited by the Company based on the achievement of the applicable performance goal(s) but which awards remain subject to time-based vesting will vest and become exercisable or payable (for clarity, to the extent of such credited portion of the award and excluding, as to an award with multiple performance goals, any portion of the award that has not been so credited (as of such termination of employment)). For avoidance of doubt and except as expressly provided in clause (b) of the preceding sentence, the foregoing is not intended to apply to any equity awards held by the Participant that are subject to performance-based vesting (which shall continue to be governed by the plan and/or award agreement applicable to such awards). Further, the foregoing is not intended to supersede any more favorable provision in any stock incentive plan and/or award agreement

regarding accelerated vesting of an equity award in the event of the Participant's termination of employment. The Committee, in its sole discretion, will determine whether any portion of an equity award has been "credited" under the terms of that award. Notwithstanding anything to the contrary herein, the post-termination exercisability of the Participant's then outstanding stock options shall continue to be governed by the stock incentive plan and stock option agreement applicable to such options.

6.5 Outplacement Services. A Participant who is a U.S. Eligible Employee as of the date of such Participant's termination of employment shall be eligible for outplacement services, provided by a vendor chosen by the Company or applicable Subsidiary and at the Company's or applicable Subsidiary's expense, after the Participant's termination of employment for up to the number of months set forth below:

- (a) Tier I Executive: 12 months
- (b) Tier II Executives: 12 months
- (c) Tier III Executive: 12 months

A Participant's right to any benefit provided under this Section 6.5 shall not be subject to liquidation or exchange for another benefit, and the amount of such benefit that the Participant receives in one taxable year shall not affect the amount of such benefits that the Participant receives in any other taxable year.

6.6 Continued Health Care Coverage. With respect to a Participant who is a U.S. Eligible Employee as of the date of such Participant's termination of employment, the Company or applicable Subsidiary shall pay to the Participant a cash payment in an amount equal to the applicable COBRA premium payments (as reasonably determined by the Administrator as of the time of Participant's termination of employment) that would be payable by the Participant to continue the Participant's company-provided medical, dental, and/or vision coverage existing as of the Participant's termination date for the number of months set forth below:

- (a) Tier I Executive: 18 months
- (b) Tier II Executives: 12 months
- (c) Tier III Executive: 12 months

For purposes of clarity, such cash payment shall be made regardless of whether the Participant actually elects coverage under COBRA, and shall be determined as of the Participant's termination of employment and not impacted by, or adjusted for, events occurring after such date (including, without limitation, changes in coverage or premiums).

6.7 Specified Employees. The provisions of this Section 6.7 shall apply if any severance payments hereunder constitute nonqualified "deferred compensation" (within the meaning of Section 409A of the Code) payable upon the Participant's Separation from Service and, in such event, such provisions shall apply only to the extent required to avoid the imputation of any tax, penalty or interest pursuant to Section 409A of the Code. It is the Company's intent that severance payments hereunder should not constitute nonqualified "deferred compensation" payable upon a Separation from Service (because such payments are intended to be exempt from Section 409A as a "short-term deferral" or separation pay due to an involuntary separation from service within the meaning of Code Section 409A or

otherwise) based on the guidance available as of the date hereof and, accordingly, should not be subject to the delayed-payment provisions set forth in this Section 6.7. Notwithstanding any other provision of the Plan to the contrary, if the Participant is a “specified employee” within the meaning of Treasury Regulation Section 1.409A-1(i) as of the date of the Participant’s Separation from Service, and the severance payments hereunder constitute non-exempt “deferred compensation” (within the meaning of Section 409A), the Participant shall not be entitled to any severance payments hereunder until the earlier of (i) the date which is six (6) months after the Participant’s Separation from Service for any reason other than death, or (ii) the date of the Participant’s death. Any amounts otherwise payable to the Participant upon or in the six (6) month period following the Participant’s Separation from Service that are not so paid by reason of this Section 6.7 shall be paid (without interest) as soon as practicable (and in all events within thirty (30) days) after the date that is six (6) months after the Participant’s Separation from Service (or, if earlier, as soon as practicable, and in all events within thirty (30) days, after the date of the Participant’s death).

7. CONDITIONS TO SEVERANCE BENEFITS

7.1 Release. Notwithstanding anything to the contrary contained herein, the Company’s or applicable Subsidiary’s obligation to pay benefits to a Participant under Section 6 is subject to the condition precedent that the Participant execute a valid and effective release of any and all claims in a form and manner acceptable to the Company, and such release is received by the Company no earlier than the Participant’s termination date, and no later than the date set forth in the release (or such other period as required by law), and such release is not revoked by the Participant (pursuant to any revocation rights afforded by applicable law) or otherwise rendered unenforceable by the Participant. Notwithstanding anything else contained herein to the contrary, the Company or applicable Subsidiary will have no obligation to pay any benefit to the Participant under the Plan unless and until that Participant’s release (in such form) has been fully executed by the Participant (and the Participant’s spouse, to the extent required by the Company), has been received by the Company, and has become effective and irrevocable by the Participant.

7.2 Departure and Entitlement Procedure. As a condition to becoming a Participant and receiving the severance benefits described in Section 6, the Executive must return and deliver to the Administrator or his or her designee all Company and Subsidiary property within seven (7) days of the Executive’s termination date. In addition, except as otherwise provided by the Company, if an Executive resigns prior to his/her scheduled termination date, then he/she shall not be entitled to any severance payments or any other severance benefits provided herein.

7.3 Other Employment. A Participant shall not be required to mitigate the amount of any payments provided for by the Plan by seeking employment or otherwise. All severance payments under the Plan shall be subject to legal deductions, and the Company and/or applicable Subsidiary reserves the right to offset the benefits payable under the Plan by any advanced monies the Participant owes the Company or a Subsidiary. In addition, in no event shall a Participant become entitled to a duplication of benefits under the Plan and any other severance plan or program of the Company or a Subsidiary. Without limiting the generality of the foregoing, in no event shall a Participant receive benefits under the Plan in connection with his or her termination of employment if such Participant is entitled to benefits under the Company’s Amended and Restated Change of Control Severance Plan in connection with such termination of employment. Notwithstanding any provision of the Plan to the contrary, to the extent that any Participant is entitled to any period of paid notice under Federal or state law including, but not limited to, the Worker Adjustment Retraining Notification Act, 29 U.S.C. Sections 2101 et seq., the benefits and amounts payable under the Plan shall be reduced (but not below zero) by the Base Pay received by the Participant during the period of such paid notice.

7.4 Limitation On Employee Rights. The Plan shall not give any employee the right to be retained in the service of the Company or to interfere with or restrict the right of the Company or applicable Subsidiary to discharge any employee at any time, with or without Cause.

8. RESOLUTION OF DISPUTES

8.1 Claim. If a Participant or any other individual (herein referred to as a "Claimant") believes that benefits under the Plan are being wrongfully denied, that the Plan is not being operated properly, or that the Claimant's legal rights are being violated with respect to the Plan, the Claimant must file a formal claim with the Administrator. Any such claim for benefits must be filed in writing within 90 days of the date upon which the Participant first knew or should have known the facts upon which the claim is based.

8.2 Claim Decision. If any claim for benefits under the Plan is denied, in whole or in part, the Claimant shall be so notified by the Administrator within thirty (30) calendar days of the date such person's claim is delivered to the Administrator. At the same time, the Administrator shall notify the Claimant of his or her right to a review by the Administrator and shall set forth, in a manner calculated to be understood by the Claimant, specific reasons for such decision, specific references to pertinent Plan provisions on which the decision is based, a description of any additional material or information necessary for the Claimant to perfect his or her request for review, an explanation of why such material or information is necessary, and an explanation of the Plan's review procedure.

8.3 Request for Review. Any Claimant or duly authorized representative may appeal from such decision by submitting to the Administrator within sixty (60) calendar days after the date of such notice of its decision a written statement:

- (a) requesting a review of the claim for benefits by the Administrator;
- (b) setting forth all of the grounds upon which the request for review is based and any facts in support thereof; and
- (c) setting forth any issues or comments which the Claimant deems relevant to the claim.

The Administrator shall act upon such appeal within sixty (60) calendar days after the latter of receipt of the Claimant's request for review by it or receipt of all additional materials reasonably requested by it from such Claimant.

8.4 Review of Decision. The Administrator shall make a full and fair review of an appeal and all written materials submitted by the Claimant in connection therewith and may require the Claimant to submit, within ten (10) calendar days of written notice by the Administrator, such additional facts, documents or other evidence as the Administrator, in its sole discretion, deems necessary or advisable in making such a review. On the basis of its review, the Administrator shall make an independent determination of the Claimant's eligibility for an allowance and the amount of such allowance, if any, under this Plan. The decision of the Administrator on any appeal shall be final and conclusive upon all persons if supported by substantial evidence in the record.

8.5 Denial on Review. If on review of a decision, the Administrator denies a claim in whole or in part, it shall give written notice of its decision to the Claimant setting forth, in a manner calculated to be understood by the Claimant, the specific reasons for such denial and specific references to the pertinent Plan provisions on which its decision was based. If a Claimant believes that the Administrator's determination on appeal is incorrect, the Claimant or duly authorized representative may invoke the

arbitration procedures described in Section 8.6 or file suit related to such determination; provided that any legal action must be taken by the Claimant within ninety (90) days after the date upon which the Administrator's written decision on review was sent to the Claimant.

8.6 Arbitration. A Claimant who has followed the procedures in Sections 8.1 through 8.5, but who has not obtained full relief on his or her claim for benefits, may, within ninety (90) days following his or her receipt of the Administrator's written decision on review pursuant to Section 8.5, apply in writing to the Administrator for expedited and binding arbitration of his or her claim in Orange County, California, before a sole arbitrator selected from Judicial Arbitration and Mediation Services, Inc., Orange County, California, or its successor ("JAMS"), or if JAMS is no longer able to supply the arbitrator, such arbitrator shall be selected from the American Arbitration Association, and shall be conducted in accordance with the provisions of California Code of Civil Procedure §§ 1280 et seq. as the exclusive forum for the resolution of such dispute. Pursuant to California Code of Civil Procedure § 1281.8, provisional injunctive relief may, but need not, be sought by the Company, a Subsidiary or an Executive in a court of law while arbitration proceedings are pending, and any provisional injunctive relief granted by such court shall remain effective until the matter is finally determined by the Arbitrator. Final resolution of any dispute through arbitration may include any remedy or relief which the Arbitrator deems just and equitable, including any and all remedies provided by applicable state or federal statutes. At the conclusion of the arbitration, the Arbitrator shall issue a written decision that sets forth the essential findings and conclusions upon which the Arbitrator's award or decision is based. Any award or relief granted by the Arbitrator hereunder shall be final and binding on the parties hereto and may be enforced by any court of competent jurisdiction. Any rights to trial by jury in any action, proceeding or counterclaim brought by any of the Company, a Subsidiary or an Executive in connection with any matter whatsoever arising out of or in any way connected with the Plan are hereby waived. The Company or applicable Subsidiary shall be responsible for payment of the forum costs of any arbitration hereunder, including the Arbitrator's fee. In any proceeding to enforce the terms of the Plan, the prevailing party shall be entitled to its or his reasonable attorneys' fees and costs (other than forum costs associated with the arbitration) incurred by it or him in connection with resolution of the dispute in addition to any other relief granted.

8.7 Legal Fees and Expenses. If any dispute arises between the parties with respect to the interpretation or performance of the Plan, the prevailing party in any arbitration or proceeding shall be entitled to recover from the other party its attorneys' fees, arbitration or court costs and other expenses incurred in connection with any such proceeding. Amounts, if any, paid to the Executive under this Section 8.7 shall be in addition to all other amounts due to the Executive pursuant to the Plan.

9. ADMINISTRATION

9.1 Administrator. Except as provided herein, the Plan shall be administered and operated by the Administrator. The Administrator is empowered to construe and interpret the provisions of the Plan and to decide all questions of eligibility for benefits under the Plan and shall make such determinations in its sole and absolute discretion. The Administrator may at any time delegate to any other named person or body, or reassume therefrom, any of its responsibilities or administrative duties with respect to the Plan.

9.2 Experts; Rules. The Administrator may contract with one or more persons to render advice with regard to any responsibility it has under the Plan. Subject to the limitations of the Plan, the Administrator shall from time to time establish such rules for the administration of the Plan as it may deem desirable.

9.3 Indemnity. The Company shall, to the extent permitted by law, by the purchase of insurance or otherwise, indemnify and hold harmless the Administrator and each other fiduciary with respect to the Plan for liabilities or expenses they and each of them incur in carrying out their respective duties under the Plan, other than for any liabilities or expenses arising out of such fiduciary's gross negligence or willful misconduct.

10. AMENDMENT

The Committee (or the Board) reserves the right to amend, suspend and/or terminate the Plan at any time in its sole discretion. No amendment, suspension or termination shall diminish benefits to which a Participant is currently entitled under the Plan. Any modification or other amendment of the Plan shall be in writing, signed by either the Company's Chief Executive Officer or Chief Human Resources Officer.

11. TAXES

Each Participant shall be solely responsible for his or her own tax liability with respect to participation in this Plan. The Company may withhold (or cause there to be withheld, as the case may be) from any amounts otherwise due or payable under or pursuant to this Plan such federal, state and local income, employment, or other taxes as may be required to be withheld pursuant to any applicable law or regulation. Notwithstanding anything else contained herein to the contrary, nothing in this Plan is intended to constitute, nor does it constitute, tax advice, and in all cases, each Participant should obtain and rely solely on the tax advice provided by the Participant's own independent tax advisors (and not this Plan, the Company, any of the Company's affiliates, or any officer, employee or agent of the Company or any of its affiliates).

12. GENERAL

12.1 Assignment by Participants. None of the benefits, payments, proceeds or claims of any Executive or Participant shall be subject to any claim of any creditor and, in particular, the same shall not be subject to attachment or garnishment or other legal process by any creditor, nor shall any such Executive have any right to alienate, anticipate, commute, pledge, encumber or assign any of the benefits or payments or proceeds that he or she may expect to receive, contingently or otherwise, under the Plan. Notwithstanding the foregoing, benefits that are in pay status may be subject to a court order of garnishment or wage assignment, or similar order, or a tax levy. The Plan shall inure to the benefit of and be enforceable by each Participant's personal or legal representatives, executors, administrators, successors, heirs, distributees, devisees, and legatees. If a Participant dies while any amount would still be payable to him or her hereunder had he or she continued to live, all such amounts, unless otherwise provided herein, shall be paid to the Participant's beneficiary in accordance with the terms of the Plan.

12.2 Binding Effect. The Company or applicable Subsidiary will require any successor (whether by purchase of assets, merger, consolidation or otherwise) to all or substantially all of the business and/or assets of the Company or applicable Subsidiary to expressly assume and agree to perform all of the obligations of the Company or applicable Subsidiary under the Plan (including the obligation to cause any subsequent successor to also assume the obligations of the Plan) unless such assumption occurs by operation of law. For avoidance of doubt, in the event that a successor of a Subsidiary (whether by purchase of assets, merger, consolidation or otherwise) assumes the Subsidiary's obligations under the Plan, the Company will have no obligations under the Plan with respect to the Executives employed by such Subsidiary.

12.3 No Waiver. No waiver of any term, provision or condition of the Plan, whether by conduct or otherwise, in any one or more instances shall be deemed or be construed as a further or continuing waiver of any such term, provision or condition or as a waiver of any other term, provision or condition of the Plan.

12.4 Expenses; Unsecured General Creditor. The benefits and costs of the Plan shall be paid by the Company and/or a Subsidiary out of its general assets. The status of a claim against the Company or a Subsidiary with respect to the benefits provided hereunder shall be same as the status of a claim against the Company or applicable Subsidiary by any general or unsecured creditor.

12.5 ERISA. The Plan is an unfunded compensation arrangement for a select group of management or highly compensated employees of the Company or a Subsidiary and any exemptions under ERISA applicable to such an arrangement shall be applicable to the Plan.

12.6 Section 409A. The Plan is intended to comply with or be exempt from Section 409A of the Code (including the Treasury Regulations and other published guidance relating thereto) so as not to subject any Participant to payment of any interest or additional tax imposed under Code Section 409A. The provisions of the Plan shall be construed and interpreted to avoid the imputation of any such additional tax, penalty or interest under Code Section 409A yet preserve (to the nearest extent reasonably possible) the intended benefit payable to the Participant.

12.7 WARN Act. Benefits payable under the Plan are intended to satisfy, where applicable, any Company obligations under the Federal Worker Adjustment and Retraining Notification Act and any similar obligations that the Company or its Subsidiaries may have under any successor or other severance pay statute.

12.8 Construction. The masculine pronoun shall include the feminine pronoun and the feminine pronoun shall include the masculine pronoun and the singular pronoun shall include the plural pronoun and the plural pronoun shall include the singular pronoun, unless the context clearly indicates otherwise.

12.9 Governing Law. The Plan shall be construed according to the laws of the State of California, except to the extent such laws are preempted by federal law.

12.10 Severability. If any provision of the Plan is held to be illegal, invalid or unenforceable under any present or future law, and if the rights or obligations of any party hereto under the Plan will not be materially and adversely affected hereby, (i) such provision will be fully severable, (ii) the Plan will be construed and enforced as if such illegal, invalid or unenforceable provision had never comprised a part hereof, (iii) the remaining provisions of the Plan will remain in full force and effect and will not be affected by the illegal, invalid or unenforceable provision or by its severance herefrom and (iv) in lieu of such illegal, invalid or unenforceable provision, there will be added automatically as a part of the Plan a legal, valid and enforceable provision as similar in terms to such illegal, invalid or unenforceable provision as may be possible.

12.11 Notices. Any notice required or permitted by the Plan shall be in writing, delivered by hand, or sent by registered or certified mail, return receipt requested, or by recognized courier service (regularly providing proof of delivery), addressed as follows:

- (a) if to the Company or, where applicable, the Administrator:

Western Digital Corporation
3355 Michelson Drive, Suite 100

Irvine, California 92612
Attention: Chief Human Resources Officer

With a copy to:

Western Digital Corporation
3355 Michelson Drive, Suite 100
Irvine, California 92612
Attention: Chief Legal Officer

(b) if to the Executive or Participant, at the most recent address set forth on the records of the Company or applicable Subsidiary, as the case may be, or to such other address or addresses most recently communicated to the Company or applicable Subsidiary by the Executive or Participant.

Each such notice shall be effective (i) if given by mail, three days after being deposited in the mails or (ii) if given personally or by other means when actually delivered at such address.

Western Digital Corporation
Computation of Ratio of Earnings to Fixed Charges

	Fiscal Year					Six Months Ended December 30, 2016
	2012	2013	2014	2015	2016	
<i>(in millions, except ratios)</i>						
Computation of earnings:						
Income before provision for income taxes	\$ 1,757	\$ 1,222	\$ 1,752	\$ 1,577	\$ 153	\$ 50
Fixed charges	47	75	75	69	285	455
Undistributed equity in income from 50%-or-less-owned affiliates	—	—	—	—	(1)	(1)
Adjusted earnings	<u>\$ 1,804</u>	<u>\$ 1,297</u>	<u>\$ 1,827</u>	<u>\$ 1,646</u>	<u>\$ 437</u>	<u>\$ 504</u>
Computation of fixed charges:						
Interest expense	\$ 33	\$ 54	\$ 56	\$ 49	\$ 266	\$ 441
Interest relating to lease guarantee of 50%-or-less-owned affiliates	—	—	—	—	—	3
Estimated interest portion of operating lease expense ⁽¹⁾	14	21	19	20	19	11
Fixed charges	<u>\$ 47</u>	<u>\$ 75</u>	<u>\$ 75</u>	<u>\$ 69</u>	<u>\$ 285</u>	<u>\$ 455</u>
Ratio of earnings to fixed charges	38.4x	17.3x	24.4x	23.9x	1.5x	1.1x

⁽¹⁾ Interest is estimated at 33% of rental charges, which considers industry benchmarks and assumption of average debt service cost over the assumed life of the related property.

**CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER
PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Stephen D. Milligan , certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Western Digital Corporation;
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 15(d)-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.

/s/ STEPHEN D. MILLIGAN

Stephen D. Milligan
Chief Executive Officer

Dated: February 7, 2017

**CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER
PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Mark P. Long , certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Western Digital Corporation;
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 15(d)-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.

/s/ MARK P. LONG

Mark P. Long

*President WD Capital, Chief Strategy Officer and Chief Financial
Officer*

Dated: February 7, 2017

The following certification is being furnished solely to accompany the Report pursuant to 18 U.S.C. § 1350 and in accordance with SEC Release No. 33-8238. This certification shall not be deemed “filed” for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, or otherwise subject to the liability of that section, nor shall it be incorporated by reference into any filing of the Company under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended, except to the extent that Western Digital Corporation specifically incorporates it by reference.

Certification of Chief Executive Officer

Pursuant to 18 U.S.C. § 1350, as created by Section 906 of the Sarbanes-Oxley Act of 2002, the undersigned officer of Western Digital Corporation, a Delaware corporation (the “Company”), hereby certifies, to his knowledge, that:

- (i) the accompanying Quarterly Report on Form 10-Q of the Company for the period ended December 30, 2016 (the “Report”) fully complies with the requirements of Section 13(a) or Section 15(d), as applicable, of the Securities Exchange Act of 1934, as amended; and
- (ii) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ STEPHEN D. MILLIGAN

Stephen D. Milligan
Chief Executive Officer

Dated: February 7, 2017

The following certification is being furnished solely to accompany the Report pursuant to 18 U.S.C. § 1350 and in accordance with SEC Release No. 33-8238. This certification shall not be deemed “filed” for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, or otherwise subject to the liability of that section, nor shall it be incorporated by reference into any filing of the Company under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended, except to the extent that Western Digital Corporation specifically incorporates it by reference.

Certification of Chief Financial Officer

Pursuant to 18 U.S.C. § 1350, as created by Section 906 of the Sarbanes-Oxley Act of 2002, the undersigned officer of Western Digital Corporation, a Delaware corporation (the “Company”), hereby certifies, to his knowledge, that:

- (i) the accompanying Quarterly Report on Form 10-Q of the Company for the period ended December 30, 2016 (the “Report”) fully complies with the requirements of Section 13(a) or Section 15(d), as applicable, of the Securities Exchange Act of 1934, as amended; and
- (ii) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ MARK P. LONG

Mark P. Long

President WD Capital, Chief Strategy Officer and Chief Financial Officer

Dated: February 7, 2017