Monotype Imaging Holdings Inc.
Form 10-Q
November 01, 2017
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended September 30, 2017

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 001-33612

MONOTYPE IMAGING HOLDINGS INC.

(Exact name of registrant as specified in its charter)

Delaware	**20-3289482**
(State of incorporation)	**(I.R.S. Employer Identification No.)**
600 Unicorn Park Drive	
Woburn, Massachusetts	**01801**
(Address of principal executive offices)	**(Zip Code)**

Registrant s telephone number, including area code: (781) 970-6000

(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, smaller reporting company or emerging growth company. See the definitions of large accelerated filer, accelerated filer , smaller reporting company and emerging growth company in Rule 12b-2 of the Exchange Act.

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

Emerging growth company

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

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

The number of shares outstanding of the registrant s common stock as of October 24, 2017 was 41,734,360.

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PART I. FINANCIAL INFORMATION

Item 1. Condensed Consolidated Financial Statements

MONOTYPE IMAGING HOLDINGS INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(Unaudited and in thousands, except share and per share data)

	September 30, 2017	December 31, 2016
Assets		
Current assets:		
Cash and cash equivalents	$ 79,540	$ 91,434
Restricted cash	5,000	
Accounts receivable, net of allowance for doubtful accounts of $598 at September 30, 2017 and $467 at December 31, 2016	30,424	26,549
Income tax refunds receivable	2,314	2,967
Prepaid expenses and other current assets	6,361	4,631
Total current assets	123,639	125,581
Property and equipment, net	16,690	14,166
Goodwill	278,487	273,489
Intangible assets, net	86,555	90,717
Restricted cash	12,990	17,992
Other assets	2,920	3,075
Total assets	$ 521,281	$ 525,020
Liabilities and Stockholders Equity		
Current liabilities:		
Accounts payable	$ 2,185	$ 2,170
Accrued expenses and other current liabilities	31,409	28,762
Accrued income taxes payable	314	1,473
Deferred revenue	16,898	16,081
Total current liabilities	50,806	48,486
Revolving line of credit	96,000	105,000
Other long-term liabilities	11,430	11,753
Deferred income taxes	38,286	37,780
Reserve for income taxes	2,685	2,727
Accrued pension benefits	6,092	5,296
Commitments and contingencies *(Note 13)*		
Stockholders equity:		

Preferred stock, $0.001 par value, Authorized shares: 10,000,000; Issued and outstanding: none				
Common stock, $0.001 par value, Authorized shares: 250,000,000; Issued: 44,822,339 at September 30, 2017 and 43,771,600 at December 31, 2016		44		43
Additional paid-in capital		292,272		274,946
Treasury stock, at cost, 3,040,769 shares at September 30, 2017 and 2,493,174 shares at December 31, 2016		(63,359)		(56,232)
Retained earnings		90,657		105,718
Accumulated other comprehensive loss		(3,632)		(10,497)
Total stockholders equity		315,982		313,978
Total liabilities and stockholders equity	$	521,281	$	525,020

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

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MONOTYPE IMAGING HOLDINGS INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited and in thousands, except share and per share data)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	**2016**	**2017**	**2016**
Revenue	$ 60,507	$ 52,229	$ 170,773	$ 150,804
Cost of revenue	9,719	8,534	28,638	24,441
Cost of revenue amortization of acquired technology	885	1,327	2,644	3,589
Total cost of revenue	10,604	9,861	31,282	28,030
Gross profit	49,903	42,368	139,491	122,774
Operating expenses:				
Marketing and selling	22,453	16,538	66,417	45,273
Research and development	8,997	7,781	27,778	21,108
General and administrative	11,291	11,353	34,032	28,840
Amortization of other intangible assets	1,021	941	3,051	2,418
Total operating expenses	43,762	36,613	131,278	97,639
Income from operations	6,141	5,755	8,213	25,135
Other (income) expense:				
Interest expense	815	429	2,365	753
Interest income	(116)	(78)	(309)	(204)
Loss on foreign exchange	1,357	360	4,544	794
Loss (gain) on derivatives	119	(93)	290	(299)
Other (income) expense, net	(32)	5	24	(16)
Total other expense	2,143	623	6,914	1,028
Income before provision for income taxes	3,998	5,132	1,299	24,107
Provision for income taxes	2,737	2,707	1,609	9,671
Net income (loss)	$ 1,261	$ 2,425	$ (310)	$ 14,436
Net income (loss) available to common stockholders basic	$ 1,196	$ 2,341	$ (310)	$ 13,982
Net income (loss) available to common stockholders diluted	$ 1,195	$ 2,340	$ (310)	$ 13,983

Net income (loss) per common share:								
Basic	$	0.03	$	0.06	$	(0.01)	$	0.36
Diluted	$	0.03	$	0.06	$	(0.01)	$	0.35
Weighted-average number of shares outstanding:								
Basic		39,594,130		39,977,120		39,576,312		39,348,437
Diluted		39,798,779		40,261,247		39,576,312		39,699,790
Dividends declared per common share	$	0.113	$	0.110	$	0.339	$	0.330

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

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MONOTYPE IMAGING HOLDINGS INC.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Unaudited and in thousands)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	**2016**	**2017**	**2016**
Net income (loss)	$ 1,261	$ 2,425	$ (310)	$ 14,436
Other comprehensive income, net of tax:				
Unrecognized actuarial gain, net of tax of $8, $4, $23 and $12, respectively	16	9	45	26
Foreign currency translation adjustments, net of tax of $1,058, $118, $3,469 and $688, respectively	2,191	131	6,820	677
Comprehensive income	$ 3,468	$ 2,565	$ 6,555	$ 15,139

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

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MONOTYPE IMAGING HOLDINGS INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited and in thousands)

	Nine Months Ended September 30, 2017	2016
Cash flows from operating activities		
Net (loss) income	$ (310)	$ 14,436
Adjustments to reconcile net (loss) income to net cash provided by operating activities:		
Depreciation and amortization	9,271	9,114
Loss on retirement of fixed assets	90	
Amortization of deferred financing costs and accreted interest	165	165
Stock based compensation	15,294	12,705
Excess tax benefit on stock options		(404)
Provision for doubtful accounts	734	216
Deferred income taxes	(2,982)	2,312
Unrealized currency loss on foreign denominated intercompany transactions	3,870	422
Changes in operating assets and liabilities:		
Accounts receivable	(3,978)	(372)
Prepaid expenses and other assets	(2,336)	(2,778)
Restricted cash	2	(9,027)
Accounts payable	(16)	(12)
Accrued income taxes payable	(349)	942
Accrued expenses and other liabilities	162	2,359
Deferred revenue	1,122	1,869
Net cash provided by operating activities	20,739	31,947
Cash flows from investing activities		
Purchases of property and equipment	(5,272)	(1,600)
Purchases of intangible asset	(54)	
Acquisition of business, net of cash acquired		(120,444)
Net cash used in investing activities	(5,326)	(122,044)
Cash flows from financing activities		
Payments on revolving line of credit	(9,000)	
Proceeds from revolving line of credit		110,000
Purchase of treasury stock	(6,446)	
Common stock dividends paid	(14,030)	(12,961)
Excess tax benefit on stock options		404
Proceeds from exercises of common stock options	1,062	2,390

Net cash (used in) provided by financing activities	(28,414)	99,833
Effect of exchange rates on cash and cash equivalents	1,107	327
(Decrease) increase in cash and cash equivalents	(11,894)	10,063
Cash and cash equivalents at beginning of period	91,434	87,520
Cash and cash equivalents at end of period	$ 79,540	$ 97,583

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

MONOTYPE IMAGING HOLDINGS INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

September 30, 2017

1. Nature of the Business

Monotype Imaging Holdings Inc. (the Company or we) empowers expression and engagement for creatives, designers, engineers and marketers at the world s most revered brands. These professionals sit at globally recognized organizations or are independent creatives located across the globe. Regardless of their organization or location, we support their efforts by producing compelling content and technologies that build beloved and valued brands, provide technology that cultivate meaningful engagement with their brand enthusiasts, and provide intelligence and insight through the measure of content performance to optimize resources and spending. Our mission is to be the first place to turn for the design assets, technology and expertise for all touchpoints. For creatives, designers and engineers, we empower expression through high-value design assets, technologies that improve the discovery, curation, measurement and brand integrity of content, and through custom studio design services. For marketers, we enable engagement with a customer s brand enthusiasts and measurement of content interactions in digital environments such as mobile messaging and social media platforms. We offer more than 99,000 typeface designs, and include some of the world s most widely used designs, such as the Times New Roman®, Helvetica®, Frutiger®, ITC Franklin Gothic , FF Meta and Droid typefaces, and support more than 250 Latin and non-Latin languages. Our e-commerce websites, including *myfonts.com, fonts.com, fontshop.com,* and *linotype.com,* which attracted more than 50 million visits in 2016 from over 200 countries and territories, offer thousands of high-quality font products from the Monotype Libraries, as well as from third parties.

We are headquartered in Woburn, Massachusetts and we operate in one business segment: the development, marketing and licensing of design assets and technology. We also maintain various offices worldwide for selling and marketing, research and development and administration. We conduct our operations through five domestic operating subsidiaries, Monotype Imaging Inc., Monotype ITC Inc., MyFonts Inc., Swyft Media Inc. and Olapic, Inc., and six wholly-owned foreign operating subsidiaries, Olapic Argentina S.A., Monotype Ltd., Monotype GmbH (Monotype Germany), Monotype Solutions India Pvt. Ltd., Monotype Hong Kong Ltd. and Monotype KK.

2. Basis of Presentation

The accompanying unaudited condensed consolidated interim financial statements as of September 30, 2017 and for the three and nine months ended September 30, 2017 and 2016 include the accounts of the Company and its wholly-owned subsidiaries and have been prepared in conformity with accounting principles generally accepted in the United States (GAAP) for interim financial reporting and pursuant to the rules and regulations of the Securities and Exchange Commission (SEC) for Quarterly Reports on Form 10-Q and Article 10 of Regulation S-X. Accordingly, such financial statements do not include all of the information and footnotes required by GAAP for complete financial statements. GAAP requires the Company s management to make estimates and assumptions that affect the amounts reported in the financial statements. Actual results could differ from those estimates. The results for interim periods are not necessarily indicative of results to be expected for the year or for any future periods. In management s opinion, these unaudited condensed consolidated interim financial statements contain all adjustments of a normal recurring nature necessary for a fair presentation of the financial statements for the interim periods presented.

These unaudited condensed consolidated interim financial statements should be read in conjunction with the Company s audited consolidated financial statements for the year ended December 31, 2016, as reported in the

Company s Annual Report on Form 10-K. The Company s significant accounting policies and practices are as described in the Annual Report, except for the adoption of Accounting Standards Update, or ASU, 2016-09, as described in Note 3 below.

3. Recently Issued Accounting Pronouncements

Adopted

Share Based Compensation

In March 2016, the Financial Accounting Standards Board, or FASB, issued ASU 2016-09, *Compensation Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting.* The guidance identifies areas for simplification involving several aspects of accounting for share based payments, including income tax consequences, classification of awards as either equity, or liabilities, an option to make a policy election to recognize gross share based compensation expense with actual forfeitures recognized as they occur as well as certain classification changes on the statement of cash flows. This guidance is effective for annual and interim reporting periods beginning after December 15, 2016, with early adoption permitted. We adopted ASU 2016-09 on January 1, 2017 and elected to account for forfeitures when they occur, on a modified retrospective basis. As a result of this adoption, $0.6 million of additional stock based compensation expense, net of tax, was recorded to retained earnings on the date of adoption as a cumulative effect adjustment related to our accounting policy change for forfeitures. In accordance with the

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adoption of this guidance, the tax effect of differences between tax deductions related to stock compensation and the corresponding financial statement expense compensation will no longer be recorded to additional paid in capital in our balance sheet. Instead, such amounts will be recorded to tax expense. We also elected to prospectively apply the change in presentation of excess tax benefits wherein excess tax benefits recognized on stock based compensation expense is now classified as an operating activity in our condensed consolidated statements of cash flows. We did not adjust the classifications of excess tax benefits in our condensed consolidated statements of cash flows for the three and nine months ended September 30, 2016. The adoption did not have any other material impact on our financial statements.

Pending

Derivatives

In August 2017, the FASB issued ASU No. 2017-12 *Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities.* This guidance simplifies the application of the hedge accounting guidance in current GAAP and improve the financial reporting of hedging relationships by allowing entities to better align their risk management activities and financial reporting for hedging relationships through changes to both designation and measurement for qualifying hedging relationships and the presentation of hedge results. Further, the new guidance allows more flexibility in the requirements to qualify and maintain hedge accounting. The new standard is effective for fiscal years beginning after December 15, 2018 and interim periods. We are currently evaluating the impact of the adoption of ASU 2017-12; however, we do not expect the adoption of this standard to have a material impact on our consolidated financial statements.

Pension Benefits

In March 2017, the FASB issued ASU No. 2017-07 *Compensation-Retirement Benefits (Topic 715)-Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost.* This guidance revises the presentation of the net periodic benefit cost in the income statement. The new standard will be effective for annual and interim periods beginning after December 15, 2017. We are currently evaluating the impact of the adoption of ASU 2017-07; however, we do not expect the adoption of this standard to have a material impact on our consolidated financial statements.

Goodwill

In January 2017, the FASB issued ASU 2017-04, *Intangibles Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment*, which eliminated step 2 from the goodwill impairment test. This guidance is effective for annual and interim reporting periods beginning after December 15, 2019, with early adoption permitted for testing dates after January 1, 2017. We are currently evaluating the impact of the adoption of ASU 2017-04; however, we do not expect the adoption of this standard to have a material impact on our consolidated financial statements.

Statement of Cash Flows

In November 2016, the FASB issued ASU 2016-18, *Statement of Cash Flows (Topic 230): Restricted Cash*, which requires companies to include amounts generally described as restricted cash and restricted cash equivalents in cash and cash equivalents when reconciling beginning-of-period and end-of-period total amounts shown on the statement of cash flows. This guidance is effective for annual and interim reporting periods beginning after December 15, 2017, with early adoption permitted. We do not expect the adoption of this guidance to have a material effect on our consolidated financial statements and related disclosures.

Leases

In February 2016, the FASB issued ASU 2016-02, *Leases (Topic 842): Amendments to the FASB Accounting Standards Codification,* which replaces the existing guidance for leases. ASU 2016-02 requires the identification of arrangements that should be accounted for as leases by lessees. In general, for lease arrangements exceeding a twelve month term, these arrangements must now be recognized as assets and liabilities on the balance sheet of the lessee. Under ASU 2016-02, a right-of-use asset and lease obligation will be recorded for all leases, whether operating or financing, while the income statement will reflect lease expense for operating leases and amortization/interest expense for financing leases. The balance sheet amount recorded for existing leases at the date of adoption of ASU 2016-02 must be calculated using the applicable incremental borrowing rate at the date of adoption. In addition, ASU 2016-02 requires the use of the modified retrospective method, which will require adjustment to all comparative periods presented in the consolidated financial statements. This guidance is effective for annual and interim periods beginning after December 15, 2018 and requires retrospective application. The Company is currently assessing the impact that adopting ASU 2016-02 will have on its consolidated financial statements and related disclosures.

Revenue Recognition

In May 2014, the FASB and the International Accounting Standards Board jointly issued ASU 2014-09, *Revenue from Contracts with Customers (Topic 606),* which outlines a comprehensive five-step revenue recognition model based on principle that replaces virtually all existing revenue recognition under U.S. GAAP and which requires revenue to be recognized in a manner to depict the transfer of promised goods or services to a customer at an amount that reflects the consideration expected to be received in exchange for those goods or services. ASU 2014-09 also provided the guidance in ASC Topic 340, *Other Assets and Deferred Costs Contracts with Customers (Subtopic 340-40)*, which includes criteria for the capitalization and amortization of certain contract acquisition and fulfillment costs. The standard requires retrospective application, however, it allows entities to choose either full retrospective adoption in which the standard is applied to all of the periods presented, or modified retrospective adoption, in which the cumulative catch-up adjustment to the opening balance of retained earnings is recognized at the date of application, with additional disclosures required to describe these effects. In August 2015, the FASB issued ASU 2015-14, *Revenue from Contracts with Customers (Topic 606): Deferral Date*, which defers the effective date of ASU 2014-09 by one year. The guidance is effective for annual reporting and interim periods beginning after December 15, 2017, with early adoption permitted for annual and interim periods beginning after December 15, 2016.

We will adopt the standard on January 1, 2018, and at that time, we will apply the modified retrospective method of adoption. We have developed an implementation plan to assess the impact of the new guidance on our operations, financial results and related disclosures. To date, we have substantially completed our initial assessment of the potential areas of the balance sheet and financial statement components impacted, have prepared our preliminary accounting policy memorandum and are beginning to assess the quantitative impact of adoption, including assessing the impact of the new guidance on our results of operations and internal controls. Based on our procedures performed to date, we have identified certain revenue streams, specifically term and royalty-based license agreements, for which the standard could have a material impact and we will continue to evaluate this assessment quarterly. Under the current guidance, revenue related to our term license agreements that are bundled with services related performance obligations for which vendor-specific objective evidence (VSOE) does not exist is required to be recognized ratably over the term of the agreement. However, under the new guidance, the Company will allocate revenue to each performance obligation in the agreement and each will require separate accounting treatment and lead to accelerated revenue recognition compared with current practice. The license portion will be recognized at the time of delivery and the service revenue will be recognized over time based on the relative standalone selling prices of each performance obligation. In addition, we have on occasion, offered extended payment terms for term licenses to our customers, including cases in which the license is delivered in full at the beginning of the contract. We currently recognize revenue under such arrangements when the payments become due, based upon the current requirement that the fee be fixed or determinable. However, under the new guidance, revenue related to such arrangements would be accelerated, with revenue related to the license recognized at the time of delivery, less a financing component (interest income) to be recognized over time based on the payment terms. Further, under the new guidance, we will be required to estimate royalty revenue from our royalty-based licenses in the period that the royalty-bearing event occurs, which is different from our current practice of recognizing royalty revenue when it is reported to us by the licensee, at which time the fee is deemed fixed or determinable. The Company has, and plans to continue to, convert printer imaging electronic OEM customers to fixed fee contracts from royalty bearing contracts. At September 30, 2017, approximately 80% of estimated printer revenue has been converted to fixed fee license contracts. The new guidance also requires certain costs related to contract acquisition, such as sales commissions, to be capitalized and amortized over the expected period of benefit. We currently recognize such expenses based on when they are earned. We are currently in the process of evaluating our commission plans and other factors that that will impact the period over which such expenses are recognized under the new guidance. We currently plan to elect the practical expedient which permits an entity to not adjust for the effects of a significant financing component if we expect that at the contract inception, the period between when the entity transfers a promised good or service to a customer and when the customer pays for

that good or service will be one year or less. We also plan to elect the practical expedient which permits an entity to only apply the transition guidance to contracts that are not completed at the date of the initial application of ASU 2014-09. We currently plan to elect the practical expedient which permits us to expense costs as they are incurred if the amortization period is determined to be one year or less.

We expect the new guidance to have a significant impact on our financial statements, including the expected transition adjustment to adopt ASC606; however, we are still in the process of evaluating the quantitative impact that the standard will have on our financial statements and related disclosures, which may be material.

Based on the progress of our evaluation to date, while we are still in the process of quantifying the transition adjustment that will be recorded on January 1, 2018, which will depend in part on the additional contracts that are executed during the fourth quarter of 2017, we anticipate that the transition adjustment to retained earnings will include approximately $5 million to $9 million of revenue from contracts entered into on or before December 31, 2017, that otherwise would have been included in 2018 revenue had ASC 606 not been adopted effective January 1, 2018. This estimate is based on contracts that have been entered into as of September 30, 2017, as well as an estimate based on our current sales forecasts, of contracts that will be entered into between October 1, 2017 and December 31, 2017. As we have not yet completed our analysis of the quantitative impact of ASC 606 on contracts with our customers, and since this estimate includes assumptions about future events that may or may not take place, actual results could differ materially from this estimate. Furthermore, as the estimate excludes several other key aspects of ASC 606, such as the changes in accounting for costs to acquire contracts, it is not intended to provide an estimate of the full transition adjustment that we will ultimately record. Finally, since the estimate excludes the potential impact of contracts entered into subsequent to January 1, 2018, it is not intended to provide a complete estimate of the impact of ASC606 on 2018 revenue.

4. Acquisition

Olapic, Inc.

On August 9, 2016, the Company purchased all of the outstanding shares of Olapic, Inc., a privately-held company located in New York, New York; its wholly-owned subsidiaries Olapic UK Ltd., based in London, England; and Olapic Argentina S.A., based in Córdoba, Argentina (collectively, Olapic). Olapic is a provider of a leading visual commerce platform for collecting, curating, showcasing and measuring crowd sourced photos and videos. Olapic s Earned Content Platform helps brands collect, curate, use and analyze user-generated content in the form of images and videos in their ecommerce experiences and across multiple marketing channels. This allows consumers to make more educated purchasing decisions, discover new products and connect to the brand s community. The Company leverages photos and videos from social network sites to help to create powerful branded experiences that drive consumer engagement and increase conversions. The Company acquired Olapic for an aggregate purchase price of

approximately $123.7 million, consisting of approximately $13.7 million in cash and borrowed $110.0 million from its line of credit, net of cash acquired. The Merger Agreement included an additional $9.0 million of consideration that has been placed in escrow and will be paid to the founders of Olapic contingent upon continued employment with the Company. Accordingly, this amount will be recognized as compensation expense over the service period contractually required to earn such amounts, which is $3.0 million after twenty four months and the remainder after thirty six months from the acquisition date. Monotype issued approximately $17.1 million of a combination of restricted stock awards or restricted stock units to the founders and employees of Olapic. These awards will vest over time based on continued employment, and accordingly will be accounted for as compensation expense. Seventy four employees from Olapic s U.S. operations, eighty four employees from Olapic s Argentina operations and forty UK and European employees joined the Company in connection with the acquisition. The results of operations of Olapic have been included in our consolidated results and revenue is included within the Creative Professional market beginning on August 9, 2016, the date of acquisition.

The table below provides the Olapic employees by functional area who joined the Company in connection with the acquisition:

	Number of employees
Marketing and selling	117
Research and development	68
General and administration	13
Total	198

The purchase price was allocated to the assets and liabilities based upon their estimated fair value at the date of acquisition, as noted below (in thousands):

		Estimated Fair Value at Acquisition Date
Cash	$	5,942
Accounts receivable and other current assets		8,174
Property and equipment and other assets		1,029
Goodwill		89,705
Identifiable intangible assets		30,100
Accounts payable and other accrued expenses		(2,468)
Deferred revenue		(7,334)
Deferred tax liability		(1,449)
Total purchase price	$	123,699

The estimated fair values of intangible assets acquired were recorded as follows:

	Estimated Fair Value at Acquisition Date (in thousands)	Estimated Useful Life (in years)
Developed technology	$ 14,300	10
Customer relationships	7,900	10
Non-compete agreements	1,400	4
Indefinite-lived intangible assets:		
Trademarks and tradenames	6,500	
Total	$ 30,100	

A portion of the purchase price has been allocated to intangible assets and goodwill, respectively, and is reflected in the tables above. The fair value of the assets acquired and liabilities assumed is less than the purchase price, resulting in the recognition of goodwill. The goodwill reflects the value of the synergies we expect to realize and the assembled workforce. The acquisition of Olapic was structured in such a manner that the goodwill is not expected to be deductible for tax purposes. The purchase price has been allocated to the tangible and intangible assets acquired and liabilities assumed based upon the respective estimates of fair value as of the date of the acquisition and using assumptions that the Company s management believes are reasonable given the information available.

We recorded revenue of $5.2 million and $13.5 million, and a net loss of $7.8 million and $24.4 million, from the acquired Olapic operations within the Company s consolidated operations for the three and nine months ended September 30, 2017, respectively. Transaction costs of $0.7 million and $1.1 million are included in general and administrative expenses in our condensed consolidated statements of operations for the three and nine months ended September 30, 2016, respectively.

Pro Forma Results

The following table shows unaudited pro forma results of operations as if we had acquired Olapic at the beginning of the periods presented (in thousands, except per share amounts):

	Three Months Ended September 30, 2016		Nine Months Ended September 30, 2016	
Revenue	$	53,586	$	159,415
Net income	$	1,116	$	4,900
Net income available to common stockholders basic	$	1,032	$	4,446
Net income available to common stock holders diluted	$	1,031	$	4,447
Net income per common share: basic	$	0.03	$	0.11
Net income per common share: diluted	$	0.03	$	0.11
Weighted average number of shares basic		39,977,120		39,348,437
Weighted average number of shares diluted		40,261,247		39,699,790

The unaudited pro forma results of operations are not necessarily indicative of the actual results that would have occurred had the transactions actually taken place at the beginning of the periods indicated.

5. Fair Value Measurements

The following table presents our financial assets and liabilities that are carried at fair value (in thousands):

	Fair Value Measurement at September 30, 2017					
	Total		Quoted Prices in Active Markets for Identical Assets (Level 1)		Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:						
Cash equivalents money market funds	$ 12,255	$	12,255	$		$
Cash equivalents commercial paper	26,672				26,672	
Cash equivalents U.S. government and agency securities	1,504		1,504			

Total short-term financial assets	40,431	13,759	26,672	
Restricted cash equivalents money market fund	9,000	9,000		
Restricted cash equivalents U.S. government and agency security fund	8,990	8,990		
Total long-term financial assets	17,990	17,990		
Total	$ 58,421	$ 31,749	$ 26,672	$

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		Fair Value Measurement at December 31, 2016		
	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Cash equivalents money market funds	$ 16,994	$ 16,994	$	$
Cash equivalents commercial paper	16,989		16,989	
Cash equivalents corporate bonds	4,802		4,802	
Cash equivalents U.S. government and agency securities	11,368	11,368		
Total short-term financial assets	50,153	28,362	21,791	
Restricted cash equivalents money market fund	9,000	9,000		
Restricted cash equivalents U.S. government and agency security fund	8,992	8,992		
Total long-term financial assets	17,992	17,992		
Total	$ 68,145	$ 46,354	$ 21,791	$

The Company s recurring fair value measures relate to short-term investments, which are classified as cash equivalents, derivative instruments and from time to time contingent consideration. The fair value of our cash equivalents is either based on quoted prices for similar assets or other observable inputs such as yield curves at commonly quoted intervals and other market corroborated inputs. The fair value of our derivatives is based on quoted market prices from various banking institutions or an independent third-party provider for similar instruments. In determining the fair value, we consider our non-performance risk and that of our counterparties. At September 30, 2017, we had one 30-day forward contract to sell 2.6 million British pounds sterling and purchase $3.4 million that together, had an immaterial fair value; and at December 31, 2016, we had one 30-day forward contract to sell 2.8 million British pounds sterling and purchase $3.4 million that together, had an immaterial fair value.

The Company s non-financial assets and non-financial liabilities subject to non-recurring measurements include goodwill and intangible assets.

6. Intangible Assets

Intangible assets consist of the following (dollar amounts in thousands):

	Weighted-Average Amortization Period (Years)	September 30, 2017 Gross Carrying Amount	Accumulated Amortization	Net Balance	December 31, 2016 Gross Carrying Amount	Accumulated Amortization	Net Balance
Customer relationships	10	$ 68,194	$ (53,419)	$ 14,775	$ 67,502	$ (50,808)	$ 16,694
Acquired technology	11	69,085	(47,840)	21,245	68,228	(44,361)	23,867

Non-compete agreements	4	14,607	(13,301)	1,306	14,440	(12,655)	1,785
Indefinite-lived intangible assets:							
Trademarks		44,829		44,829	43,971		43,971
Domain names		4,400		4,400	4,400		4,400
Total		$ 201,115	$ (114,560)	$ 86,555	$ 198,541	$ (107,824)	$ 90,717

7. Debt

On September 15, 2015, the Company entered into a new credit agreement (the New Credit Agreement) by and among the Company, the Company s subsidiary, Monotype Imaging Inc., any financial institution that becomes a Lender (as defined therein) and Silicon Valley Bank, as agent which provides for a five-year $150.0 million secured revolving credit facility (the Credit Facility). The Credit Facility permits the Company to request that the Lenders, at their election, increase the secured credit facility to a maximum of $200.0 million. The Credit Facility is available to the Company on a revolving basis through September 15, 2020.

Repayment of any amounts borrowed are not required until maturity of the Credit Facility. However, the Company may repay any amounts borrowed at any time, without premium or penalty. At September 30, 2017 and December 31, 2016, the Company had $96.0 million and $105.0 million outstanding under the Credit Facility. At September 30, 2017 and December 31, 2016, available borrowings under the Credit Facility have been reduced by approximately $0.5 million for one standby letter of credit issued in connection with a facility lease agreement, leaving $53.5 million and $44.5 million available for borrowing at September 30, 2017 and December 31, 2016, respectively.

Borrowings under the Credit Facility bear a variable rate not less than zero based upon, at the Company s option, either LIBOR or the higher of (i) the prime rate as published in the Wall Street Journal, and (ii) 0.5% plus the overnight federal funds rate, plus in each case, an applicable margin. The applicable margin for LIBOR loans, based on the applicable leverage ratio, is 1.25%, 1.50% or 1.75% per annum, and the applicable margin for base rate loans, based on the applicable leverage ratio, is either 0.25%, 0.50% or 0.75% per annum. At September 30, 2017, our rate, inclusive of applicable margins, was 2.8% for LIBOR, and at December 31, 2016, our rate, inclusive of applicable margins, was 2.5% for LIBOR.

As of September 30, 2017, the maximum leverage ratio permitted was 3.00:1.00 and our leverage ratio was 2.47:1.00 and the minimum fixed charge coverage ratio was 1.25:1.00 and our fixed charge ratio was 6.57:1.00. Failure to comply with these covenants, or the occurrence of an event of default, could permit the Lenders under the New Credit Agreement to declare all amounts borrowed under the New Credit Agreement, together with accrued interest and fees, to be immediately due and payable. In addition, the Credit Facility is secured by a lien on substantially all of the Company s and its domestic subsidiaries tangible and intangible property by a pledge of all of the equity interests of the Company s direct and indirect domestic subsidiaries and by a pledge by the Company s domestic subsidiaries of 65% of the equity of their direct foreign subsidiaries, subject to limited exceptions. In addition to other covenants, the New Credit Agreement places limits on the Company and its subsidiaries ability to incur debt or liens and engage in sale-leaseback transactions, make loans and investments, incur additional indebtedness, engage in mergers, acquisitions and asset sales, transact with affiliates and alter its business. The Company was in compliance with the covenants under the Credit Facility as of September 30, 2017.

8. Defined Benefit Pension Plan

Our German subsidiary maintains an unfunded defined benefit pension plan which covers substantially all employees who joined the company prior to the plan s closure to new participants in 2006. Participants are entitled to benefits in the form of retirement, disability and surviving dependent pensions. Benefits generally depend on years of service and the salary of the employees.

The components of net periodic benefit cost included in the accompanying condensed consolidated statements of operations were as follows (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
Service cost	$ 25	$ 23	$ 71	$ 71
Interest cost	29	31	81	91
Amortization	24	13	68	38
Net periodic benefit cost	$ 78	$ 67	$ 220	$ 200

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9. Income Taxes

A reconciliation of income taxes computed at federal statutory rates to income tax expense is as follows (dollar amounts in thousands):

	Three Months Ended September 30,			
	2017		2016	
Provision for income taxes at statutory rate	$ 1,399	35.0%	$ 1,796	35.0%
State and local income taxes, net of federal tax benefit	(173)	(4.3)%	559	10.9%
Stock based compensation	141	3.5%	86	1.7%
Foreign rate differential	(109)	(2.7)%	(255)	(4.9)%
Research credits	(381)	(9.5)%	(141)	(2.8)%
Permanent non-deductible acquisition-related expense	1,629	40.7%	905	17.6%
Disqualifying dispositions on incentive stock options			(33)	(0.6)%
Net shortfall on stock based compensation	257	6.4%		
Other, net	(26)	(0.6)%	(210)	(4.2)%
Reported income tax provision	$ 2,737	68.5%	$ 2,707	52.7%

	Nine Months Ended September 30,			
	2017		2016	
Provision for income taxes at statutory rate	$ 455	35.0%	$ 8,437	35.0%
State and local income taxes, net of federal tax benefit	(234)	(18.0)%	830	3.4%
Stock based compensation	64	5.0%	181	0.8%
Foreign rate differential	(47)	(3.6)%	(512)	(2.1)%
Research credits	(170)	(13.1)%	(300)	(1.2)%
Permanent non-deductible acquisition-related expense	727	55.9%	1,324	5.5%
Disqualifying dispositions on incentive stock options			(44)	(0.2)%
Net shortfall on stock based compensation	799	61.5%		
Other, net	15	1.2%	(245)	(1.1)%
Reported income tax provision	$ 1,609	123.9%	$ 9,671	40.1%

At September 30, 2017, the reserve for uncertain tax positions was approximately $6.5 million. Of this amount, $4.0 million is recorded as a reduction of deferred tax assets and $2.5 million is classified as long-term liabilities.

10. Net Income Per Share

For the three and nine months ended September 30, 2017 and 2016, the net income (loss) available to common shareholders is divided by the weighted average number of common shares outstanding during the period to calculate diluted earnings per share. The assumed exercise of stock options and assumed vesting of restricted stock and restricted stock units were included in the computation of net income per share for the three months ended September 30, 2017, but were excluded in the computation of net (loss) per share for the nine months ended

September 30, 2017, as their effect would have been anti-dilutive. For the three months ended September 30, 2017 and for the three and nine months ended September 30, 2016, the two-class method was used in the computation of diluted net income (loss) per share, as the result was more dilutive.

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The following presents a reconciliation of the numerator and denominator used in the calculation of basic net income (loss) per share and, a reconciliation of the numerator and denominator used in the calculation of diluted net income (loss) per share (in thousands, except share and per share data):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
Numerator:				
Net income (loss), as reported	$ 1,261	$ 2,425	$ (310)	$ 14,436
Less: net income attributable to participating securities	(65)	(84)		(454)
Net income (loss) available to common shareholders basic	$ 1,196	$ 2,341	$ (310)	$ 13,982
Denominator:				
Basic:				
Weighted-average shares of common stock outstanding	41,750,884	41,687,590	41,700,355	40,730,524
Less: weighted-average shares of unvested restricted common stock outstanding	(2,156,754)	(1,710,470)	(2,124,043)	(1,382,087)
Weighted-average number of common shares used in computing basic net income (loss) per common share	39,594,130	39,977,120	39,576,312	39,348,437
Net income (loss) per share applicable to common shareholders basic	$ 0.03	$ 0.06	$ (0.01)	$ 0.36

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
Numerator:				
Net income (loss) available to common shareholders basic	$ 1,196	$ 2,341	$ (310)	$ 13,982
Add-back: undistributed earnings allocated to unvested shareholders	(179)	(88)		33
Less: undistributed earnings reallocated to unvested shareholders	178	87		(32)

Net income (loss) available to common shareholders diluted	$	1,195	$	2,340	$	(310)	$	13,983
Denominator:								
Diluted:								
Weighted-average shares of common stock outstanding		41,750,884		41,687,590		41,700,355		40,730,524
Less: weighted-average shares of unvested restricted common stock outstanding		(2,156,754)		(1,710,470)		(2,124,043)		(1,382,087)
Weighted-average number of common shares issuable upon exercise of outstanding stock options, based on the treasury stock method		204,649		284,127				351,353
Weighted-average number of common shares used in computing diluted net income (loss) per common share		39,798,779		40,261,247		39,576,312		39,699,790
Net income (loss) per share applicable to common shareholders diluted	$	0.03	$	0.06	$	(0.01)	$	0.35

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The following common share equivalents have been excluded from the computation of diluted weighted-average shares outstanding, as their effect would have been anti-dilutive:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
Options	633,858	776,827	824,536	700,934
Unvested restricted stock	566,934	357,338	652,741	354,379
Unvested restricted stock units	32,971	15,873	58,674	14,681

11. Stockholders Equity

Share Purchases

On August 30, 2016, the Company s Board of Directors approved a share purchase program permitting repurchases of up to $25.0 million of the Company s outstanding shares of common stock through December 31, 2017. During the quarter ended September 30, 2017, the Company repurchased a total of 232,989 shares of its common stock for an aggregate purchase price of $4.2 million, including brokers fees. Intended to offset shareholder dilution, the Company expects to make repurchases periodically, either on the open market or in privately negotiated transactions, subject to availability, as business and market conditions warrant. The share repurchase program does not obligate the Company to acquire any particular amount of common stock, and the program may be suspended or discontinued at management s and/or the Board of Directors discretion.

Share Based Compensation

We account for share based compensation in accordance with ASC Topic No. 718, *Compensation Stock Compensation*, which requires the measurement of compensation costs at fair value on the date of grant and recognition of compensation expense over the service period for awards expected to vest. The following presents the impact of share based compensation expense on our condensed consolidated statements of operations (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
Marketing and selling	$ 2,455	$ 2,164	$ 7,348	$ 5,349
Research and development	1,131	1,180	3,227	2,869
General and administrative	1,685	1,962	4,719	4,487
Total expensed	$ 5,271	$ 5,306	$ 15,294	$ 12,705
Property and equipment	44		97	
Total share based compensation	$ 5,315	$ 5,306	$ 15,391	$ 12,705

In the three and nine months ended September 30, 2017, $44 thousand and $97 thousand, respectively, of share based compensation was capitalized as part of internal software projects, and this amount is included in property and equipment, net in our condensed consolidated balance sheet.

As of September 30, 2017, the Company had $42.7 million of unrecognized share based compensation expense related to employees and directors unvested stock option awards, restricted stock units and restricted stock awards that are expected to be recognized over a weighted-average period of 2.6 years.

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12. Segment Reporting

We view our operations and manage our business as one segment: the development, marketing and licensing of technologies and fonts. Factors used to identify our single segment include the financial information available for evaluation by our chief operating decision maker in making decisions about how to allocate resources and assess performance. While our technologies and services are sold into two principal markets, Creative Professional and OEM, expenses and assets are not formally allocated to these market segments, and operating results are assessed on an aggregate basis to make decisions about the allocation of resources. The following table presents revenue for these two principle markets (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
Creative Professional	$ 34,521	$ 27,798	$ 92,234	$ 75,170
OEM	25,986	24,431	78,539	75,634
Total	$ 60,507	$ 52,229	$ 170,773	$ 150,804

Geographic segment information

Effective as of January 1, 2017, our presentation of geographic revenue has been changed to better align with how our business operates. As a result, we now report revenue based on the geographic location of our customers, rather than based on the location of our subsidiary receiving such revenue. For example, licenses may be sold to large international companies which may be headquartered in the Republic of Korea, but the sales are received and recorded by our subsidiary located in the United States. Historically, in the table below such revenues would be included in the revenue for the United States, whereas for our new presentation, such revenues would be reported in the Republic of Korea and included in the revenue for Rest of World. Geographic revenue for the three months and nine months ended September 30, 2016 has been recast to conform to this presentation.

We market our products and services principally through offices in the U.S., United Kingdom, Germany, China, Republic of Korea and Japan. The following table summarizes revenue by customer location (in thousands of dollars, except percentages):

	Three Months Ended September 30,			
	2017		2016	
	Sales	% of Total	Sales	% of Total
	(In thousands, except percentages)			
United States	$ 27,951	46.2%	$ 25,129	48.1%
Japan	14,963	24.7	12,187	23.3
Europe, Middle East, and Africa (EMEA)	13,952	23.1	9,971	19.1
Rest of World	3,641	6.0	4,942	9.5
Total	$ 60,507	100.0%	$ 52,229	100.0%

	Nine Months Ended September 30,			
	2017		2016	
	Sales	% of Total	Sales	% of Total
	(In thousands, except percentages)			
United States	$ 74,631	43.7%	$ 64,125	42.5%
Japan	44,278	25.9	38,872	25.8
Europe, Middle East, and Africa (EMEA)	37,392	21.9	32,215	21.4
Rest of World	14,472	8.5	15,592	10.3
Total	$ 170,773	100.0%	$ 150,804	100.0%

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Long-lived assets, which include property and equipment, goodwill and intangible assets, but exclude other assets and deferred tax assets, are attributed to geographic areas in which Company assets reside and is shown below (in thousands):

	September 30, 2017	December 31, 2016
Long-lived assets:		
United States	$ 316,048	$ 318,786
United Kingdom	4,050	3,882
Germany	57,563	52,237
Rest of World	4,071	3,467
Total	$ 381,732	$ 378,372

13. Commitments and Contingencies

Legal Proceedings

From time to time, we may be a party to various claims, suits and complaints. We do not believe that there are claims or legal proceedings that, if determined adversely to us, would have a material adverse effect on our business, results of operations or financial condition.

Licensing Warranty

Under our standard license agreement with our OEM customers, we warrant that the licensed technologies are free of infringement claims of intellectual property rights and will meet the specifications as defined in the licensing agreement for a specified period, typically one year. Under the licensing agreements, liability for such indemnity obligations is limited, generally to the total arrangement fee; however, exceptions have been made on a case-by-case basis, increasing the maximum potential liability to agreed upon amounts at the time the contract is entered into or unlimited liability. We have never incurred costs payable to a customer or business partner to defend lawsuits or settle claims related to these warranties, and as a result, management believes the estimated fair value of these warranties is minimal. Accordingly, there are no liabilities recorded for these warranties as of September 30, 2017 and December 31, 2016.

14. Subsequent Events

Dividend Declaration

On October 26, 2017 the Company s Board of Directors declared a $0.113 per share quarterly cash dividend on our outstanding common stock. The record date is set for January 2, 2018 and the dividend is payable to shareholders of record on January 22, 2018. Dividends are declared at the discretion of the Company s Board of Directors and depend on actual cash from operations, the Company s financial condition and capital requirements and any other factors the Company s Board of Directors may consider relevant. Future dividend declarations, as well as the record and payment dates for such dividends, will be determined by the Company s Board of Directors on a quarterly basis.

Share Purchase Program

Subsequent to September 30, 2017, the Company purchased 8,000 shares of common stock for $0.2 million, at an average price per share of $19.63 through October 24, 2017. The Company purchased these shares on the open market at prevailing market prices and in accordance with its previously announced share purchase program. At October 24, 2017, $12.8 million remains for future purchase under the Plan.

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

Forward Looking Statements and Projections

This Quarterly Report on Form 10-Q contains forward-looking statements. Forward-looking statements relate to future events or our future financial performance. We generally identify forward-looking statements by terminology such as may, will, should, expects, plans, anticipates, could, intends, target, projects, contemplates, believes, estimates, predicts, potential or continue or the negative of these terms or other similar words. These statements are only predictions. We have based these forward-looking statements largely on our current expectations and projections about future events and financial

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trends that we believe may affect our business, results of operations and financial condition. The outcome of the events described in these forward looking statements is subject to risks, uncertainties and other factors described in Management s Discussion and Analysis of Financial Condition and Results of Operations, Risk Factors and elsewhere in this Quarterly Report on Form 10-Q. Accordingly, you should not rely upon forward-looking statements as predictions of future events. We cannot assure you that the events and circumstances reflected in the forward-looking statements will be achieved or occur, and actual results could differ materially from those projected in the forward-looking statements. The forward-looking statements made in this Quarterly Report on Form 10-Q relate only to events as of the date on which the statements are made. We undertake no obligation to update any forward-looking statement to reflect events or circumstances after the date on which the statement is made or to reflect the occurrence of unanticipated events.

Overview

Monotype empowers expression and engagement for creatives, designers, engineers and marketers at the world s most revered brands. These professionals sit at globally recognized organizations or are independent creatives located across the globe. Regardless of their organization or location, we support their efforts by producing compelling content and technologies that build beloved and valued brands, provide technology that cultivate meaningful engagement with their brand enthusiasts, and provide intelligence and insight through the measure of content performance to optimize resources and spending.

Our mission is to be the first place to turn for the design assets, technology and expertise for all touchpoints.

For creatives, designers and engineers, we empower expression through high-value design assets, technologies that improve the discovery, curation, measurement and brand integrity of content, and through custom studio design services. For marketers, we enable engagement with a customer s brand enthusiasts and measurement of content interactions in digital environments such as mobile messaging and social media platforms.

We offer more than 99,000 typeface designs, and include some of the world s most widely used designs, such as the Times New Roman®, Helvetica®, Frutiger®, ITC Franklin Gothic , FF Meta and Droid typefaces, and support more than 250 Latin and non-Latin languages. Our e-commerce websites, including *myfonts.com, fonts.com, fontshop.com,* and *linotype.com,* which attracted more than 50 million visits in 2016 from over 200 countries and territories, offer thousands of high-quality font products from the Monotype Libraries, as well as from third parties.

Sources of Revenue

We derive revenue from two principal sources: licensing our fonts and technology to brands and creative professionals, which we refer to as our Creative Professional revenue, and licensing our text imaging solutions to consumer device manufacturers and independent software vendors, which we refer to as our OEM revenue. We derive our Creative Professional revenue primarily from brands, agencies, publishers, corporations, enterprises, small businesses and individuals. We derive our OEM revenue primarily from consumer device manufacturers. Some of our revenue streams, particularly project-related and custom revenue where spending is largely discretionary in nature, have historically been, and we expect them to continue to be in the future, susceptible to weakening economic conditions.

Effective as of January 1, 2017, our presentation of geographic revenue has been changed to better align with our business operates. As a result, we now report revenue based on the geographic location of our customers, rather than based on the location of our subsidiary receiving such revenue. For example, licenses may be sold to large international companies which may be headquartered in the Republic of Korea, but the sales are received and recorded

by our subsidiary located in the United States. Historically, such revenues would be included in the revenue for the United States in the table below, whereas for our new presentation, such revenues would be reported in the Republic of Korea and included in the revenue for Rest of World in the table below. Geographic revenue for the three months and nine months ended September 30, 2016, has been recast to conform to this presentation.

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We market our products and services principally through offices in the U.S., United Kingdom, Germany, China, Republic of Korea and Japan. The following summarizes revenue by customer location (in thousands of dollars, except percentages):

	Three Months Ended September 30,			
	2017		2016	
	Sales	% of Total	Sales	% of Total
	(In thousands, except percentages)			
United States	$ 27,951	46.2%	$ 25,129	48.1%
Japan	14,963	24.7	12,187	23.3
Europe, Middle East, and Africa (EMEA)	13,952	23.1	9,971	19.1
Rest of World	3,641	6.0	4,942	9.5
Total	$ 60,507	100.0%	$ 52,229	100.0%

	Nine Months Ended September 30,			
	2017		2016	
	Sales	% of Total	Sales	% of Total
	(In thousands, except percentages)			
United States	$ 74,631	43.7%	$ 64,125	42.5%
Japan				

964.0	992.7	(3)	1	
Other Countries & Corporate	**202.5**	226.3	(11)	(6)
Total	**$ 4,093.6**	$ 4,411.1	(7)	
Franchised revenues				
U.S.	**$ 956.5**	$ 899.4	6	6
Europe	**707.8**	681.8	4	11
APMEA	**161.9**	150.6	8	10
Other Countries & Corporate	**126.9**	124.4	2	10
Total	**$ 1,953.1**	$ 1,856.2	5	9
Total revenues				
U.S.	**$ 2,049.7**	$ 2,084.4	(2)	(2)
Europe	**2,541.7**	2,688.9	(5)	6
APMEA	**1,125.9**	1,143.3	(2)	2
Other Countries & Corporate	**329.4**	350.7	(6)	
Total	**$ 6,046.7**	$ 6,267.3	(4)	2

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REVENUES

Dollars in millions

Nine Months Ended September 30,	2009	2008	% Inc / (Dec)	% Inc / (Dec) Excluding Currency Translation
Company-operated sales				
U.S.	**$ 3,252.2**	$ 3,490.1	(7)	(7)
Europe	**4,899.2**	5,752.3	(15)	3
APMEA	**2,740.9**	2,801.9	(2)	5
Other Countries & Corporate	**536.2**	661.6	(19)	(8)
Total	**$ 11,428.5**	$ 12,705.9	(10)	
Franchised revenues				
U.S.	**$ 2,718.1**	$ 2,557.1	6	6
Europe	**1,854.7**	1,918.4	(3)	10
APMEA	**442.0**	431.7	2	14
Other Countries & Corporate	**328.0**	344.3	(5)	9
Total	**$ 5,342.8**	$ 5,251.5	2	8
Total revenues				
U.S.	**$ 5,970.3**	$ 6,047.2	(1)	(1)
Europe	**6,753.9**	7,670.7	(12)	5
APMEA	**3,182.9**	3,233.6	(2)	6
Other Countries & Corporate	**864.2**	1,005.9	(14)	(2)
Total	**$ 16,771.3**	$ 17,957.4	(7)	3

The Company continues to optimize its restaurant ownership mix, cash flow and returns through its refranchising strategy. The shift to a greater percentage of franchised restaurants negatively impacts consolidated revenues as Company-operated sales shift to franchised sales, where we receive rent and/or royalties. In addition, there is a corresponding decrease in Company-operated margin dollars and an increase in franchised margin dollars. The impact on margin percentages varies based on sales and operating costs of refranchised restaurants.

Consolidated revenues decreased 4% (increased 2% in constant currencies) for the quarter and decreased 7% (increased 3% in constant currencies) for the nine months. The constant currency growth was driven by positive comparable sales in all segments, partly offset by the impact of the refranchising strategy in certain of the Company s major markets. As a result of refranchising, franchised restaurants represent 80% of systemwide restaurants at September 30, 2009 compared with 79% at September 30, 2008.

In the U.S., the decrease in revenues for the quarter and nine months was due to the impact of the refranchising strategy, partly offset by an increase in comparable sales. New products, including the Angus Third Pounder and McCafé premium coffees, as well as core products and value offerings drove comparable sales.

In Europe, the constant currency increase in revenues for the quarter and nine months was primarily due to strong comparable sales in the U.K., France and Russia (which is entirely Company-operated). These increases were partly offset by the impact of the refranchising strategy, primarily in the U.K. and Germany.

In APMEA, the constant currency increase in revenues for the quarter and nine months was primarily driven by strong comparable sales in Australia and certain Asian markets as well as expansion in China, partly offset by negative comparable sales in China.

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The following table presents the percent change in comparable sales for the quarters and nine months ended September 30, 2009 and 2008:

COMPARABLE SALES	% Increase			
	Quarters Ended		Nine Months Ended	
	September 30,		September 30,*	
	2009	2008	**2009**	2008
U.S.	**2.5**	4.7	**3.5**	3.7
Europe	**5.8**	8.2	**5.4**	8.8
APMEA	**2.2**	7.8	**4.0**	8.6
Other Countries & Corporate	**6.1**	13.6	**5.1**	13.6
Total	**3.8**	7.1	**4.3**	6.8

* On a consolidated basis, comparable guest counts increased 1.3% and 3.3% for the nine months ended September 30, 2009 and 2008, respectively.

The following table presents the percent change in Systemwide sales for the quarter and nine months ended September 30, 2009:

SYSTEMWIDE SALES	Quarter Ended		Nine Months Ended	
	September 30, 2009		September 30, 2009	
	% Inc / (Dec)	% Inc Excluding Currency Translation	% Inc / (Dec)	% Inc Excluding Currency Translation
U.S.	3	3	4	4
Europe	(1)	8	(7)	8
APMEA	9	6	5	8
Other Countries & Corporate	(1)	8	(6)	7
Total	2	6		6

The following tables present franchised sales, which are not recorded in the income statement, and the related percentage change for the quarters and nine months ended September 30, 2009 and 2008:

FRANCHISED SALES

Dollars in millions

Quarters Ended September 30,	2009	2008	% Inc	% Inc Excluding Currency Translation
U.S.	**$ 6,948.8**	$ 6,597.2	5	5
Europe	**4,027.7**	3,935.4	2	10
APMEA	**2,578.4**	2,271.9	13	8
Other Countries & Corporate	**1,558.5**	1,544.0	1	10
Total*	**$ 15,113.4**	$ 14,348.5	5	7

* Included $3,046.6 million and $2,866.7 million of sales in 2009 and 2008, respectively, derived from developmental licensee restaurants or foreign affiliated markets where the Company earns a royalty based on sales. The remaining balance of franchised sales is derived from conventional franchised restaurants where the Company earns rent and royalties based on sales.

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FRANCHISED SALES

Dollars in millions

Nine Months Ended September 30,	2009	2008	% Inc / (Dec)	% Inc Excluding Currency Translation
U.S.	**$ 20,011.3**	$ 18,794.9	6	6
Europe	**10,608.6**	10,983.1	(3)	10
APMEA	**7,159.4**	6,584.7	9	9
Other Countries & Corporate	**4,088.5**	4,277.7	(4)	9
Total*	**$ 41,867.8**	$ 40,640.4	3	8

* Included $8,527.3 million and $8,103.0 million of sales in 2009 and 2008, respectively, derived from developmental licensee restaurants or foreign affiliated markets where the Company earns a royalty based on sales. The remaining balance of franchised sales is derived from conventional franchised restaurants where the Company earns rent and royalties based on sales.

Restaurant Margins

FRANCHISED AND COMPANY-OPERATED RESTAURANT MARGINS

Dollars in millions

Quarters Ended September 30,	Percent		Amount		% Inc / (Dec)	% Inc / (Dec) Excluding Currency Translation
	2009	2008	**2009**	2008		
Franchised						
U.S.	**83.4**	83.7	**$ 797.4**	$ 753.0	6	6
Europe	**79.5**	79.7	**562.6**	543.6	3	11
APMEA	**89.5**	89.7	**144.9**	135.1	7	9
Other Countries & Corporate	**86.4**	86.6	**109.6**	107.6	2	10
Total	**82.7**	82.9	**$ 1,614.5**	$ 1,539.3	5	8
Company-operated						
U.S.	**19.3**	18.2	**$ 211.3**	$ 216.1	(2)	(2)
Europe	**20.4**	20.0	**374.7**	400.7	(6)	7
APMEA	**18.0**	17.0	**173.5**	168.4	3	7
Other Countries & Corporate	**16.9**	17.1	**34.3**	38.7	(11)	(7)
Total	**19.4**	18.7	**$ 793.8**	$ 823.9	(4)	4

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FRANCHISED AND COMPANY-OPERATED RESTAURANT MARGINS

Dollars in millions

Nine Months Ended September 30,	Percent		Amount		% Inc / (Dec)	% Inc / (Dec) Excluding Currency Translation
	2009	2008	**2009**	2008		
Franchised						
U.S.	**83.1**	83.2	**$ 2,259.3**	$ 2,127.0	6	6
Europe	**78.3**	78.7	**1,451.7**	1,509.7	(4)	9
APMEA	**89.7**	89.3	**396.6**	385.4	3	13
Other Countries & Corporate	**86.0**	86.4	**281.9**	297.4	(5)	8
Total	**82.2**	82.3	**$ 4,389.5**	$ 4,319.5	2	8
Company-operated						
U.S.	**19.1**	18.4	**$ 620.9**	$ 640.9	(3)	(3)
Europe	**18.2**	18.1	**889.7**	1,040.2	(14)	2
APMEA	**16.7**	16.4	**457.6**	458.8		8
Other Countries & Corporate	**15.1**	15.7	**80.7**	104.0	(22)	(12)
Total	**17.9**	17.7	**$ 2,048.9**	$ 2,243.9	(9)	1

Franchised margin dollars increased $75.2 million or 5% ($126.3 million or 8% in constant currencies) for the quarter and $70.0 million or 2% ($341.5 million or 8% in constant currencies) for the nine months. Positive comparable sales in every segment and the refranchising strategy were the primary drivers of the constant currency growth in franchised margin dollars in both periods.

In the U.S., the franchised margin percent for the quarter and nine months reflected positive comparable sales offset by additional depreciation related to the Company s investment in the beverage initiative.

In Europe, the franchised margin percent for the quarter and nine months was negatively impacted by the refranchising strategy and higher occupancy expenses partly offset by positive comparable sales. In addition, the cost of strategic brand and sales building initiatives, primarily in the U.K. and Germany, negatively impacted the nine months.

In APMEA, the decrease in the franchised margin percent for the quarter was primarily driven by higher occupancy expenses in Australia, partly offset by a benefit from foreign currency translation, mostly due to the stronger Japanese yen and the weaker Australian dollar. The franchised margin percent for the nine months was higher than the prior year primarily due to the impact of foreign currency translation.

Company-operated margin dollars decreased $30.1 million or 4% (increased $30.1 million or 4% in constant currencies) for the quarter and decreased $195.0 million or 9% (increased $25.5 million or 1% in constant currencies) for the nine months. In both periods Company-operated margin dollars were negatively impacted by the refranchising strategy. The refranchising strategy had a positive impact on the margin percent for both periods.

In the U.S., the Company-operated margin percent increased for the quarter and nine months due to positive comparable sales and the impact of the refranchising strategy, partly offset by additional depreciation related to the beverage initiative and higher commodity costs. The quarter also benefited from lower employee benefit costs.

Europe s Company-operated margin percent increased for the quarter and nine months due to positive comparable sales and refranchising, partly offset by higher commodity and labor costs. Local inflation and the impact of weaker currencies on the cost of certain imported products drove higher costs, primarily in Russia, and negatively impacted the Company-operated margin percent for the quarter and nine months.

In APMEA, the Company-operated margin percent increased for the quarter primarily due to lower commodity and other costs in China, partly offset by higher labor costs throughout the segment. The margin percent increased for the nine months primarily due to positive comparable sales in many markets partly offset by higher commodity and labor costs.

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The following table presents margin components as a percent of sales:

CONSOLIDATED COMPANY-OPERATED RESTAURANT EXPENSES AND MARGINS AS A PERCENT OF SALES

	Quarters Ended September 30,		Nine Months Ended September 30,	
	2009	2008	**2009**	2008
Food & paper	**33.1**	33.8	**33.8**	33.5
Payroll & employee benefits	**25.1**	25.3	**25.6**	26.1
Occupancy & other operating expenses	**22.4**	22.2	**22.7**	22.7
Total expenses	**80.6**	81.3	**82.1**	82.3
Company-operated margins	**19.4**	18.7	**17.9**	17.7

Selling, General & Administrative Expenses

Selling, general & administrative expenses decreased 6% (2% in constant currencies) for the quarter and decreased 9% (3% in constant currencies) for the nine months. Costs in 2008 related to the Beijing Summer Olympics impacted both periods and costs from the Company s biennial Worldwide Owner/Operator Convention in second quarter 2008 impacted the nine months. Selling, general & administrative expenses as a percent of revenues decreased to 9.4% for the nine months 2009 compared with 9.7% for 2008, and as a percent of Systemwide sales, decreased to 3.0% for 2009 compared with 3.2% for 2008.

Other Operating (Income) Expense, Net

OTHER OPERATING (INCOME) EXPENSE, NET

In millions

	Quarters Ended September 30,		Nine Months Ended September 30,	
	2009	2008	**2009**	2008
Gains on sales of restaurant businesses	**$ (32.5)**	$ (30.5)	**$ (78.6)**	$ (73.8)
Equity in earnings of unconsolidated affiliates	**(54.9)**	(42.3)	**(118.2)**	(91.8)
Asset dispositions and other (income) expense	**14.8**	30.2	**41.2**	54.1
Total	**$ (72.6)**	$ (42.6)	**$ (155.6)**	$ (111.5)

Equity in earnings of unconsolidated affiliates for the quarter and nine months reflected increased income from Japan.

Operating Income

OPERATING INCOME

Dollars in millions

Quarters ended September 30,	**2009**	2008	% Inc	% Inc Excluding Currency Translation
U.S.	**$ 865.6**	$ 815.5	6	6

Europe	**770.9**	769.1		10
APMEA	**279.2**	234.1	19	21
Other Countries & Corporate	**17.1**	5.0	n/m	n/m
Total	**$ 1,932.8**	$ 1,823.7	6	11

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OPERATING INCOME

Dollars in millions

Nine Months Ended September 30,	2009	2008	% Inc / (Dec)	% Inc Excluding Currency Translation
U.S.	**$ 2,426.0**	$ 2,294.3	6	6
Europe	**1,879.7**	2,018.1	(7)	7
APMEA	**723.4**	642.9	13	21
Other Countries & Corporate	**(14.4)**	(14.6)	1	n/m
Total	**$ 5,014.7**	$ 4,940.7	1	9

n/m Not meaningful

In the U.S., operating results increased for the quarter and nine months primarily due to higher franchised margin dollars.

In Europe, constant currency operating results for the quarter and nine months reflected strong operating performance in France, the U.K. and Russia.

In APMEA, constant currency operating results for the quarter and nine months were driven primarily by strong results in Australia. Expansion and improved cost controls in China also contributed to results for both periods.

Combined Operating Margin

Combined operating margin is defined as operating income as a percent of total revenues. Combined operating margin for the nine months 2009 and 2008 was 29.9% and 27.5%, respectively. In constant currencies, the 2009 combined operating margin increased 180 basis points.

Interest Expense

Interest expense for the quarter and nine months decreased primarily due to lower average interest rates, partly offset by higher average debt levels. Weaker foreign currencies benefited the nine months and, to a lesser extent, the quarter.

Nonoperating (Income) Expense, Net

NONOPERATING (INCOME) EXPENSE, NET

In millions

	Quarters Ended September 30,		Nine Months Ended September 30,	
	2009	2008	**2009**	2008
Interest income	**$ (4.4)**	$ (16.0)	**$ (14.7)**	$ (68.7)
Translation and hedging activity	**(6.8)**	8.1	**(31.9)**	0.5
Other expense	**5.2**	1.1	**12.2**	1.7
Total	**$ (6.0)**	$ (6.8)	**$ (34.4)**	$ (66.5)

Interest income declined for the quarter and nine months primarily due to lower interest rates. Interest income in the nine months 2008 included interest on the partial recovery of prior years sales taxes in the U.K.

Translation and hedging activity for 2009 included gains on the hedging of certain foreign-denominated cash flows.

Other expense for the quarter and nine months ended 2008 reflected higher income from the Company s minority interest in Redbox, which was sold in February 2009.

Gain on Sale of Investment

In 2009, the Company sold its minority ownership interest in Redbox to Coinstar, Inc., the majority owner, for total consideration of $139.8 million. In connection with the sale, in February, the Company received initial consideration valued at $51.6 million consisting of 1.5 million shares of Coinstar common stock at an agreed to value of $41.6 million and $10 million in cash with the balance of the purchase price deferred. In April, the Company sold all of its holdings in the Coinstar common stock for $46.8 million. In second quarter, the Company received $78.4 million in cash from Coinstar as deferred consideration, and in third quarter, the Company received $9.8 million in cash from Coinstar as final consideration.

As a result of the transaction, the Company recognized a nonoperating pretax gain of $0.6 million in the third quarter 2009 and $94.9 million for the nine months.

In second quarter 2008, the Company sold its minority ownership interest in U.K.-based Pret A Manger. As a result of the sale, the Company received cash proceeds of $229.4 million and recognized a nonoperating pretax gain of $160.1 million.

Income Taxes

The effective income tax rate was 30.3% for the nine months 2009 compared with 30.1% for the nine months 2008, and 30.8% for third quarter 2009 compared with 29.9% for third quarter 2008.

Cash Flows and Financial Position

The Company generates significant cash from operations and has substantial credit capacity to fund operating and discretionary spending such as capital expenditures, debt repayments, dividends and share repurchases.

Cash provided by operations totaled $4.4 billion and exceeded capital expenditures by $3.1 billion for the nine months 2009. Cash provided by operations decreased $73.9 million compared with the first nine months of 2008 primarily due to changes in working capital items, partly due to the receipt of $142.7 million in 2008 related to the completion of an Internal Revenue Service examination and higher incentive based compensation payments in 2009 for the 2008 performance year.

Cash used for investing activities totaled $1.1 billion for the nine months 2009, an increase of $123.8 million over the first nine months of 2008, as a result of lower proceeds from sales of investments and properties and higher expenditures for purchases of restaurant businesses, partly offset by lower capital expenditures due to the impact of foreign currencies.

Cash used for financing activities totaled $3.2 billion for the nine months 2009, a decrease of $708.6 million compared with the first nine months of 2008. Financing activities in 2009 reflected lower treasury stock purchases, partly offset by higher dividends and lower proceeds from stock option exercises.

Debt obligations at September 30, 2009 totaled $11.1 billion compared with $10.2 billion at December 31, 2008. The increase in 2009 was primarily due to net issuances of $645 million and the impact of changes in exchange rates on foreign currency denominated debt of $192 million. In October 2009, the Company repaid about $400 million of debt that matured.

Accounting Changes

Fair Value Measurements

In 2006, the Financial Accounting Standards Board (FASB) issued guidance in the Fair Value Measurements and Disclosures Topic of the FASB Accounting Standards Codification (ASC). This guidance defines fair value, establishes a framework for measuring fair value in accordance with generally accepted accounting principles, and expands disclosures about fair value measurements. This guidance does not require any new fair value measurements; rather, it applies to other accounting pronouncements that require or permit fair value measurements. The provisions of the guidance, as issued, were effective January 1, 2008. However, in February 2008, the FASB deferred the effective date for one year for certain non-financial assets and non-financial liabilities, except those that are recognized or disclosed at fair value in the financial statements on a recurring basis (i.e., at least annually). The Company adopted the required provisions related to debt and derivatives as of January 1, 2008 and adopted the remaining required provisions for non-financial assets and liabilities as of January 1, 2009. The effect of adoption was not significant in either period.

Derivative Instruments and Hedging Activities

In March 2008, the FASB issued guidance on disclosures in the Derivatives and Hedging Topic of the FASB ASC. This guidance amends and expands the previous disclosure requirements surrounding accounting for derivative instruments and hedging activities to provide more qualitative and quantitative information on how and why an entity uses derivative instruments, how derivative instruments and related hedged items are accounted for, and how derivative instruments and related hedged items affect an entity s financial position, financial performance and cash flows. The Company adopted the disclosure requirements as of January 1, 2009 on a prospective basis; accordingly, disclosures related to interim periods prior to the date of adoption have not been presented. The adoption had no impact on our consolidated financial statements,

besides the additional disclosures.

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Interim Disclosures about Fair Value of Financial Instruments

In April 2009, the FASB issued guidance on interim disclosures about fair value in the Financial Instruments Topic of the FASB ASC. This guidance requires a publicly traded company to include disclosures about the fair value of its financial instruments whenever it issues summarized financial information for interim reporting periods. The Company adopted the guidance for the second quarter 2009. The adoption had no impact on our consolidated financial statements, besides the additional disclosure.

Subsequent Events

In May 2009, the FASB issued guidance in the Subsequent Events Topic of the FASB ASC. This guidance requires disclosure of the date through which an entity has evaluated subsequent events and the basis for that date. The Company adopted the guidance for the second quarter 2009. The adoption had no impact on our consolidated financial statements, besides the additional disclosure.

Recently Issued Accounting Standards

In June 2009, the FASB issued amendments to the guidance on variable interest entities and consolidation. This guidance modifies the method for determining whether an entity is a variable interest entity as well as the methods permitted for determining the primary beneficiary of a variable interest entity. In addition, this guidance requires ongoing reassessments of whether a company is the primary beneficiary of a variable interest entity and enhanced disclosures related to a company s involvement with a variable interest entity. The Company expects to adopt this guidance effective January 1, 2010, as required. The Company is currently evaluating the impact of adopting this guidance and does not expect the adoption to have a significant impact to its consolidated financial statements.

Risk Factors and Cautionary Statement Regarding Forward-Looking Statements

This report includes forward-looking statements about our plans and future performance, including those under Outlook. These statements use such words as may, will, expect, believe and plan. They reflect our expectations and speak only as of the date of this report. We do not unde to update them. Our expectations (or the underlying assumptions) may change or not be realized, and you should not rely unduly on forward-looking statements.

Our business and execution of our strategic plan, the Plan to Win, are subject to risks. The most important of these is our ability to remain relevant to our customers and a brand they trust. Meeting customer expectations is complicated by the risks inherent in our operating environment. The informal eating out (IEO) segment of the restaurant industry, although largely mature in our major markets, is highly fragmented and competitive. The current economic environment has caused the IEO segment to contract in many markets, including some of our major markets, and this may continue. The current economic environment has increased consumer focus on value, heightening pricing pressures across the industry, which could affect our ability to continue to grow sales despite the strength of our Brand and value proposition. We have the added challenge of the cultural, economic and regulatory differences that exist among the more than 100 countries where we operate. Regulatory and similar initiatives around the world have also become more wide-ranging and prescriptive and affect how we operate and our results. In particular, increasing focus on nutritional content and on the production, processing and preparation of food from field to front counter presents challenges for our Brand.

The risks we face can have an impact both in the near- and long-term and are reflected in the following considerations and factors that we believe are most likely to affect our performance.

Our ability to remain a relevant and trusted brand and to increase sales depends largely on how well we execute the Plan to Win, particularly as the global economy emerges from recession.

The Plan to Win addresses the key drivers of our business and results people, products, place, price and promotion. The quality of our execution depends mainly on the following:

Our ability to anticipate and respond effectively to trends or other factors that affect the IEO segment and our competitive position in the diverse markets we serve, such as spending patterns, demographic changes, trends in food preparation, consumer preferences and publicity about our products, all of which can drive popular perceptions of our business or affect the willingness of other companies to enter into site, supply or other arrangements or alliances with us;

The success of our initiatives to support menu choice, physical activity and nutritional awareness and to address these and other matters of social responsibility in a way that communicates our values effectively and inspires trust and confidence;

Our ability to respond effectively to adverse perceptions about the quick-service segment of the IEO segment, our products and promotions (including the premiums we offer, such as our Happy Meal toys) or the reliability of our supply chain and the safety of the ingredients we use, and our ability to manage the potential impact on McDonald s of food-borne illnesses or product safety issues;

The success of our plans to improve existing products and to roll out new products and product line extensions, as well as the impact of our competitors actions, including in response to our product improvements and introductions, and our ability to continue robust product development and manage the complexity of our restaurant operations;

Our ability to achieve an overall product mix that differentiates the McDonald s experience and balances consumer value with margin expansion, particularly in markets where pricing or cost pressures are significant or have been exacerbated by challenging economic conditions;

The impact of our pricing, marketing and promotional plans on sales and margins and our ability to adjust our plans to respond quickly to changing economic conditions;

The impact of events such as boycotts or protests, labor strikes and supply chain interruptions (including due to lack of supply or price increases) that can adversely affect us directly or adversely affect the vendors, franchisees and others that are also part of the McDonald s System and whose performance has a material impact on our results;

Our ability to recruit and retain qualified local personnel to manage our operations and growth in certain developing markets;

Our ability to drive restaurant improvements and to motivate our restaurant personnel to achieve sustained high service levels so as to improve consumer perceptions of our ability to meet expectations for quality food served in clean and friendly environments;

Whether our restaurant remodeling and rebuilding efforts, which remain a priority notwithstanding the current period of slow economic growth and challenging credit markets, is targeted at the elements of the restaurant experience that will best accomplish our goals to enhance the relevance of our Brand and achieve an efficient allocation of our capital resources;

Our ability to maintain alignment with franchisees on operating, promotional and capital-intensive initiatives;

The risks to our Brand if a franchisee defaults in its obligations (particularly requirements to pay royalties, make capital investments and open new restaurants), experiences food safety or other operational problems or projects a brand image inconsistent with our values, all of which are more significant risks if a franchisee controls a large number of restaurants as is the case in Latin America; and

Our ability to leverage promotional or operating successes in individual markets into other markets in a timely and cost-effective way.

Our results and financial condition are affected by global and local market conditions, which can adversely affect our sales, margins and net income.

Our results of operations are substantially affected not only by global economic conditions, but also by local operating and economic conditions, which can vary substantially by market. Unfavorable conditions can depress sales in a given market or daypart (e.g., breakfast). To mitigate the impact of these conditions, we may take promotional or other actions that adversely affect our margins, limit our operating flexibility or result in charges, restaurant closings or sales of Company-operated restaurants. Some macroeconomic conditions could have an even more wide-ranging and prolonged impact. The current environment has been characterized by slowing economies, rising unemployment, declining wages, constrained credit and volatile financial markets. These conditions have significantly affected consumer spending and habits. Moreover, the timing and strength of a recovery is uncertain in many of our most important markets, and growth in consumer spending generally lags improvement in the broader economy. The key factors that affect our ability to manage the impact of these conditions are the following:

Whether our strategies will permit us to compete effectively and make continued market share gains, while at the same time achieving sales and operating income within our targeted long-term average annual range of growth;

The effectiveness of our supply chain management, including hedging strategies, to preserve and, where possible, expand our margins;

Our ability to manage the impact of fluctuations in foreign exchange rates, which are expected to adversely affect full year 2009 results, changes in interest rates and governmental actions to manage national economic conditions such as credit availability, consumer spending, unemployment levels and inflation rates;

The impact on our margins of labor costs given our labor-intensive business model, the long-term trend toward higher wages in both mature and developing markets and the potential impact of union organizing efforts on day-to-day operations of our restaurants;

Whether we are able to identify and develop restaurant sites consistent with our plans for net growth of Systemwide restaurants from year to year, and whether new sites are as profitable as expected;

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The challenges and uncertainties associated with operating in developing markets, such as China, Russia and India, which may entail a relatively higher risk of political instability, economic volatility, crime, corruption and social and ethnic unrest, all of which are exacerbated in many cases by a lack of an independent and experienced judiciary and uncertainties in how local law is applied and enforced, including in areas most relevant to commercial transactions and foreign investment; and

The nature and timing of decisions about underperforming markets or assets, including decisions that result in impairment charges that reduce our earnings.

Increasing regulatory complexity will continue to affect our operations and results in material ways.

Our legal and regulatory environment worldwide exposes us to complex compliance, litigation and similar risks that affect our operations and results in material ways. In many of our markets, including the United States and Europe, we are subject to increasing regulation, which has increased our cost of doing business. In developing markets, we face the risks associated with new and untested laws and judicial systems. Among the more important regulatory and litigation risks we face and must manage are the following:

The cost, compliance and other risks associated with the often conflicting regulations we face, especially in the United States where inconsistent standards imposed by local, state and federal authorities can adversely affect popular perceptions of our business and increase our exposure to litigation or governmental investigations or proceedings, and the impact of new, potential or changing regulation that affects or restricts elements of our business, particularly those relating to advertising to children, nutritional content and product labeling and safety;

The impact of nutritional, health and other scientific inquiries and conclusions, which constantly evolve and often have contradictory implications, but nonetheless drive popular opinion, litigation and regulation in ways that could be material to our business;

The risks and costs of McDonald s nutritional labeling and other disclosure practices, particularly given differences among applicable legal requirements and practices within the restaurant industry with respect to testing and disclosure, ordinary variations in food preparation among our own restaurants, and the need to rely on the accuracy and completeness of information obtained from third party suppliers;

The risks and costs to us, our franchisees and our supply chain of increased focus by U.S. and overseas governmental authorities on environmental matters, such as climate change, the reduction of greenhouse gases and water consumption, including as a result of initiatives that effectively impose a tax on carbon emissions, such as the proposed cap and trade legislation pending in the U.S. Congress;

The impact of litigation trends, particularly in our major markets, including class actions, labor and employment claims and landlord/tenant disputes, the relative level of our defense costs, which vary from period to period depending on the number, nature and procedural status of pending proceedings; and the cost and other effects of settlements or judgments, which may require us to make disclosures or take other actions that may affect perceptions of our Brand and products;

Adverse results of pending or future litigation, including litigation challenging the composition of our products, or the appropriateness or accuracy of our advertising or other communications;

The increasing costs and other effects of compliance with U.S. and overseas regulations affecting our workforce and labor practices, including regulations relating to wage and hour practices, immigration, mandatory healthcare benefits and unlawful workplace discrimination;

The impact of the current economic conditions on unemployment levels and consumer confidence and the effect of initiatives to stimulate economic recovery and to further regulate financial markets on the cost and availability of funding for the Company and its franchisees, inflation and foreign exchange rates;

Disruptions in our operations or price volatility in a market that can result from governmental actions, such as price or import-export controls, increased tariffs or government-mandated closure of our or our vendors operations, and the cost and disruption of responding to governmental investigations or proceedings, whether or not they have merit;

The risks associated with information security and the use of cashless payments, such as increased investment in technology, the costs of compliance with privacy, consumer protection and other laws, the impact on our margins as the use of cashless payments increases, the potential costs associated with alleged security breaches and the loss of consumer confidence that may result; and

The impact of changes in financial reporting requirements, accounting principles or practices, related legal or regulatory interpretations or our critical accounting estimates, changes in tax accounting or tax laws (or interpretations thereof), and the impact of settlements of adjustments proposed by the IRS or other taxing authorities in connection with our tax audits, all of which will depend on their timing, nature and scope.

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The trading volatility and price of our common stock may be affected by many factors.

Many factors affect the volatility and price of our common stock in addition to our operating results and prospects. The most important of these, some of which are outside our control, are the following:

- The current uncertain global economic conditions and market volatility;

- Governmental action or inaction in light of key indicators of economic activity or events that can significantly influence financial markets, particularly in the United States which is the principal trading market for our common stock, and media reports and commentary about economic or other matters, even when the matter in question does not directly relate to our business;

- Trading activity in our common stock or trading activity in derivative instruments with respect to our common stock or debt securities, which can reflect market commentary (including commentary that may be unreliable or incomplete in some cases) or expectations about our business, our creditworthiness or investor confidence generally; actions by shareholders and others seeking to influence our business strategies; sales of large blocks of our stock or portfolio rebalancing activities by significant shareholders; or trading activity that results from the ordinary course rebalancing of stock indices in which McDonald s may be included, such as the S&P 500 Index and the Dow Jones Industrial Average;

- The impact of our stock repurchase program, dividend rate or changes in our debt levels on our credit ratings, interest expense, ability to obtain funding on favorable terms or our operating or financial flexibility, especially if lenders impose new operating or financial covenants; and

- The impact on our results of other corporate actions, such as those we may take from time to time as part of our continuous review of our corporate structure in light of business, legal and tax considerations.

Our results and financial condition are affected by our ownership mix.

Our refranchising strategy involves a shift to a greater percentage of franchised restaurants. The decision to own restaurants or to operate under franchise or license agreements is driven by many factors whose interrelationship is complex and changing. When we refranchise a restaurant, it reduces consolidated revenues as Company-operated sales shift to franchised sales, where we receive rent and/or royalties. It also reduces Company-operated margin dollars while increasing franchised margin dollars, with the impact on margin percentages varying based on sales and operating costs of the refranchised restaurants. Our refranchising strategy can also expose us to risks, including the following:

- Whether the franchisees we select will have the experience and financial resources in the relevant markets to be effective operators of McDonald s restaurants;

- Potential ongoing payment obligations as a result of our retention of any contingent liabilities in connection with refranchising transactions, such as the indemnification obligations we may incur as a result of the Latam transaction; and

- The risk that our contractual and other rights and remedies to protect against defaults by our counterparties will be limited by local law, costly to exercise or otherwise subject to limitations or litigation that may impair our ability to prevent or mitigate any adverse impact on our Brand or on the financial performance we expect under our franchising and developmental license agreements.

Our results can be adversely affected by disruptions or events, such as the impact of severe weather conditions and natural disasters.

Severe weather conditions, terrorist activities, health epidemics or pandemics or the prospect of these events can have an adverse impact on consumer spending and confidence levels or on other factors that affect our results and prospects, such as commodity costs. Our receipt of proceeds under any insurance we maintain with respect to certain of these risks may be delayed or the proceeds may be insufficient to offset our losses fully.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

There were no material changes to the disclosure made in our Annual Report on Form 10-K for the year ended December 31, 2008 regarding this matter.

Item 4. Controls and Procedures

An evaluation was conducted under the supervision and with the participation of the Company s management, including the Chief Executive Officer (CEO) and Chief Financial Officer (CFO), of the effectiveness of the design and operation of the Company s disclosure controls and procedures as of September 30, 2009. Based on that evaluation, the CEO and CFO concluded that the Company s disclosure controls and procedures were effective as of such date to ensure that information required to be disclosed in the reports that it files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms. Such officers also confirm that there was no change in the Company s internal control over financial reporting during the quarter ended September 30, 2009 that has materially affected, or is reasonably likely to materially affect, the Company s internal control over financial reporting.

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PART II OTHER INFORMATION

Item 1. Legal Proceedings

Allergens

Plaintiffs have filed numerous complaints against the Company (and in some instances our franchisee or a franchisee s operating company), alleging that McDonald s misrepresented its french fries and hash browns as free of wheat, gluten and/or milk, when the french fries and hash browns allegedly contain derivatives of wheat, gluten and/or milk. The complaints include claims for violation of state consumer fraud acts, unfair competition or deceptive trade practices acts, strict liability, failure to warn, negligence, breach of express and implied warranties, fraud and fraudulent concealment, negligent misrepresentation and concealment, unjust enrichment, and false advertising. They seek to recover unspecified compensatory and punitive damages, restitution and disgorgement of profits, and attorneys fees.

A number of these cases are pending in the Federal District Court for the Northern District of Illinois. Some of the cases pending in the Northern District of Illinois have been combined into one action that seeks to form a national class of consumers, generally defined as individuals who purchased McDonald s french fries and hash browns and who have allergies or sensitivities to consumption of wheat and/or dairy products. The first case of this type, *Debra Moffatt v. McDonald s Corporation* (MDL Case No. 06-cv-4467), was filed on February 17, 2006. On May 6, 2009, the Court denied the consolidated plaintiffs motion for class certification. The other cases pending in the Northern District of Illinois seek damages only for an individual plaintiff or a minor child on whose behalf the action was brought and have been transferred and assigned to the same federal judge.

The previously identified case that was pending in the Circuit Court of Palm Beach County, Florida, *Annalise Chimiak v. McDonald s Corporation and R&L Partnership* (Case No. 2006CA3337), has been resolved. The remainder of the cases (all of which seek damages only for individual plaintiffs) have been resolved, with the exception of one case involving three individual plaintiffs who are each only seeking damages on an individual basis, which is pending in state court in Illinois.

The Company believes that it has substantial legal and factual defenses to the plaintiffs claims and intends to defend its interests vigorously.

Item 1A. Risk Factors

This report contains certain forward-looking statements which reflect management s expectations regarding future events and operating performance and speak only as of the date hereof. These forward-looking statements involve a number of risks and uncertainties. These and other risks are noted in the Risk Factors and Cautionary Statement Regarding Forward-Looking Statements following Management s Discussion and Analysis.

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

Issuer Purchases of Equity Securities*

The following table presents information related to repurchases of common stock the Company made during the three months ended September 30, 2009:

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Programs (1)	Approximate Dollar Value of Shares that May Yet Be Purchased Under the Programs (1)
July 1-31, 2009	5,351,928	$56.53	5,351,928	$2,505,898,000
August 1-31, 2009	4,910,273	$55.62	4,910,273	$2,232,802,000
September 1-30, 2009	3,276,732	$55.84	3,276,732	$2,049,821,000
Total	13,538,933	$56.03	13,538,933	(1)

*

Subject to applicable law, the Company may repurchase shares directly in the open market, in privately negotiated transactions, or pursuant to derivative instruments and plans complying with Rule 10b5-1, among other types of transactions and arrangements.

(1) On September 12, 2007, the Company s Board of Directors approved a share repurchase program that authorized the purchase of up to $10 billion of the Company s outstanding common stock with no specified expiration date (2007 Program). On September 24, 2009, the Company s Board of Directors terminated the 2007 Program, effective October 1, 2009, and replaced it with a new share repurchase program that authorizes the purchase of up to $10 billion of the Company s outstanding common stock with no specified expiration date (2009 Program). As of September 30, 2009, no further share repurchases may be made under the 2007 Program; future share repurchases will be made pursuant to the 2009 Program.

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Item 6. Exhibits

Exhibit Number		Description
(3)	(a)	Restated Certificate of Incorporation, effective as of March 24, 1998, incorporated herein by reference from Form 8-K, dated April 17, 1998.
	(b)	By-Laws, as amended and restated with effect as of December 4, 2008, incorporated herein by reference from Form 8-K, dated December 4, 2008.
(4)		Instruments defining the rights of security holders, including Indentures: *
	(a)	Senior Debt Securities Indenture, incorporated herein by reference from Exhibit (4)(a) of Form S-3 Registration Statement (File No. 333-14141), filed October 15, 1996.
	(b)	Subordinated Debt Securities Indenture, incorporated herein by reference from Exhibit (4)(b) of Form S-3 Registration Statement (File No. 333-14141), filed October 15, 1996.
	(c)	Debt Securities Indenture, incorporated herein by reference from Exhibit (4)(a) of Form S-3 Registration Statement (File No. 33-12364), filed March 3, 1987.
(10)		Material Contracts
	(a)	Directors Deferred Compensation Plan, effective as of January 1, 2008, incorporated herein by reference from Form 8-K, dated November 28, 2007.**
	(b)	McDonald s Excess Benefit and Deferred Bonus Plan, effective January 1, 2008, as amended and restated July 8, 2008, incorporated herein by reference from Form 10-Q, for the quarter ended June 30, 2008.**
		(i) First Amendment to the McDonald s Excess Benefit and Deferred Bonus Plan, effective as of October 21, 2008, incorporated herein by reference from Form 10-Q, for the quarter ended September 30, 2008.**
	(c)	McDonald s Corporation Supplemental Profit Sharing and Savings Plan, effective as of September 1, 2001, incorporated herein by reference from Form 10-K, for the year ended December 31, 2001.**
		(i) First Amendment to the McDonald s Corporation Supplemental Profit Sharing and Savings Plan, effective as of January 1, 2002, incorporated herein by reference from Form 10-K, for the year ended December 31, 2002.**
		(ii) Second Amendment to the McDonald s Corporation Supplemental Profit Sharing and Savings Plan, effective January 1, 2005, incorporated herein by reference from Form 10-K, for the year ended December 31, 2004.**
	(d)	1975 Stock Ownership Option Plan, as amended and restated July 30, 2001, incorporated herein by reference from Form 10-Q, for the quarter ended September 30, 2001.**
		(i) First Amendment to McDonald s Corporation 1975 Stock Ownership Option Plan, as amended and restated, effective as of February 14, 2007, incorporated herein by reference from Form 10-Q, for the quarter ended March 31, 2007.**
	(e)	1992 Stock Ownership Incentive Plan, as amended and restated January 1, 2001, incorporated herein by reference from Form 10-Q, for the quarter ended March 31, 2001.**
		(i) First Amendment to McDonald s Corporation 1992 Stock Ownership Incentive Plan, as amended and restated, effective as of February 14, 2007, incorporated herein by reference from Form 10-Q, for the quarter ended March 31, 2007.**
	(f)	1999 Non-Employee Director Stock Option Plan, as amended and restated September 12, 2000, incorporated herein by reference from Form 10-Q, for the quarter ended September 30, 2000.**
	(g)	McDonald s Corporation Executive Retention Replacement Plan, effective as of December 31, 2007 (as amended and restated on December 31, 2008), incorporated herein by reference from Form 10-K, for the year ended December 31, 2008.**
	(h)	McDonald s Corporation Amended and Restated 2001 Omnibus Stock Ownership Plan, effective July 1, 2008, incorporated herein by reference from Form 10-Q for the quarter ended June 30, 2009.**

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(i) First amendment to the McDonald s Corporation Amended and Restated 2001 Omnibus Stock Ownership Plan, incorporated herein by reference from Form 10-K, for the year ended December 31, 2008.**

(i) Form of McDonald s Corporation Tier I Change of Control Employment Agreement, incorporated herein by reference from Form 10-Q, for the quarter ended September 30, 2008.**

(j) McDonald s Corporation 2009 Cash Incentive Plan, effective as of May 27, 2009, incorporated herein by reference from Form 10-Q for the quarter ended June 30, 2009.**

(k) Form of Stock Option Grant Notice, incorporated herein by reference from Form 10-Q, for the quarter ended June 30, 2005.**

(l) Form of Restricted Stock Unit Award Notice, incorporated herein by reference from Form 10-Q, for the quarter ended June 30, 2005.**

(m) McDonald s Corporation Severance Plan, effective January 1, 2008, incorporated by reference from Form 8-K, dated November 28, 2007.**

(i) First Amendment of McDonald s Corporation Severance Plan, effective as of October 1, 2008, incorporated herein by reference from Form 10-Q, for the quarter ended September 30, 2008.**

(n) Employment Contract between Denis Hennequin and the Company, dated February 26, 2007, incorporated herein by reference from Form 10-K, for the year ended December 31, 2006.**

(o) Amended Assignment Agreement between Timothy Fenton and the Company, dated January 2008, incorporated herein by reference from Form 10-Q, for the quarter ended March 31, 2008.**

(i) 2009 Amendment to the Amended Assignment Agreement between Timothy Fenton and the Company, effective as of January 1, 2009, incorporated herein by reference from Form 10-Q, for the quarter ended March 31, 2009.**

(p) Relocation Agreement between Timothy Fenton and the Company, dated January 12, 2006, incorporated herein by reference from Form 10-K, for the year ended December 31, 2006.**

(q) Description of Restricted Stock Units granted to Andrew J. McKenna, incorporated herein by reference from Form 10-Q for the quarter ended June 30, 2009.**

(r) Terms of the Restricted Stock Units granted pursuant to the Company s Amended and Restated 2001 Omnibus Stock Ownership Plan, incorporated herein by reference from Form 10-Q, for the quarter ended June 30, 2008.**

(s) McDonald s Corporation Target Incentive Plan, effective as of January 1, 2008, incorporated herein by reference from Form 8-K, dated January 23, 2008.**

(t) Terms of equity compensation awards granted in the European Union pursuant to the Company s Amended and Restated 2001 Omnibus Stock Ownership Plan, incorporated herein by reference from Form 10-Q, for the quarter ended March 31, 2008.**

(12)	Computation of ratio of earnings to fixed charges.
(31.1)	Rule 13a-14(a) Certification of Chief Executive Officer.
(31.2)	Rule 13a-14(a) Certification of Chief Financial Officer.
(32.1)	Certification pursuant to 18 U.S.C. Section 1350 by the Chief Executive Officer, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
(32.2)	Certification pursuant to 18 U.S.C. Section 1350 by the Chief Financial Officer, 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.***

* Other instruments defining the rights of holders of long-term debt of the registrant and all of its subsidiaries for which consolidated financial statements are required to be filed and which are not required to be registered with the Commission, are not included herein as the securities authorized under these instruments, individually, do not exceed 10% of the total assets of the registrant and its subsidiaries on a consolidated basis. An agreement to furnish a copy of any such instruments to the Commission upon request has been filed with the Commission.

** Denotes compensatory plan.

*** In accordance with Regulation S-T, the XBRL-related information in Exhibit 101 to this Quarterly Report on Form 10-Q shall be deemed to be furnished and not filed .

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SIGNATURE

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

McDONALD S CORPORATION

(Registrant)

November 5, 2009

/s/ Peter J. Bensen
Peter J. Bensen
Corporate Executive Vice President and

Chief Financial Officer

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