STARBUCKS CORP
Form 10-Q
April 29, 2014
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549
FORM 10-Q

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the Quarterly Period Ended March 30, 2014
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: 0-20322
Starbucks Corporation
(Exact Name of Registrant as Specified in its Charter)

Washington	91-1325671
(State or Other Jurisdiction of Incorporation or Organization)	(IRS Employer Identification No.)

2401 Utah Avenue South, Seattle, Washington 98134
(Address of principal executive offices)
(206) 447-1575
(Registrant's Telephone Number, including Area Code)
Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No ¨
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No ¨
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act): Yes ¨ No x
Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Title	Shares Outstanding as of April 23, 2014
Common Stock, par value $0.001 per share	752.8 million

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PART I — FINANCIAL INFORMATION
Item 1. Financial Statements
STARBUCKS CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF EARNINGS
(in millions, except per share data)
(unaudited)

	Quarter Ended		Two Quarters Ended	
	Mar 30, 2014	Mar 31, 2013	Mar 30, 2014	Mar 31, 2013
Net revenues:				
Company-operated stores	$3,068.0	$2,807.7	$6,411.8	$5,797.3
Licensed stores	356.2	322.1	758.0	672.2
CPG, foodservice and other	449.6	419.8	943.6	873.2
Total net revenues	3,873.8	3,549.6	8,113.4	7,342.7
Cost of sales including occupancy costs	1,629.2	1,530.4	3,424.2	3,151.1
Store operating expenses	1,134.5	1,038.4	2,309.6	2,127.9
Other operating expenses	110.9	105.8	225.8	231.9
Depreciation and amortization expenses	174.4	153.1	344.1	302.0
General and administrative expenses	240.6	230.3	483.2	462.2
Litigation charge/(credit)	—	—	(20.2)	—
Total operating expenses	3,289.6	3,058.0	6,766.7	6,275.1
Income from equity investees	59.9	52.5	111.0	107.0
Operating income	644.1	544.1	1,457.7	1,174.6
Interest income and other, net	17.8	50.8	37.6	48.0
Interest expense	(16.7)	(6.1)	(31.3)	(12.7)
Earnings before income taxes	645.2	588.8	1,464.0	1,209.9
Income taxes	218.3	198.1	496.4	386.8
Net earnings including noncontrolling interests	426.9	390.7	967.6	823.1
Net earnings/(loss) attributable to noncontrolling interests	(0.1)	0.3	—	0.6
Net earnings attributable to Starbucks	$427.0	$390.4	$967.6	$822.5
Earnings per share - basic	$0.57	$0.52	$1.28	$1.10
Earnings per share - diluted	$0.56	$0.51	$1.26	$1.08
Weighted average shares outstanding:				
Basic	755.2	749.1	755.0	747.6
Diluted	764.6	761.3	765.4	761.3
Cash dividends declared per share	$0.26	$0.21	$0.52	$0.42

See Notes to Condensed Consolidated Financial Statements

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STARBUCKS CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(in millions, unaudited)

	Quarter Ended		Two Quarters Ended	
	Mar 30, 2014	Mar 31, 2013	Mar 30, 2014	Mar 31, 2013
Net earnings including noncontrolling interests	$426.9	$390.7	$967.6	$823.1
Other comprehensive income/(loss), net of tax:				
Unrealized holding gains/(losses) on available-for-sale securities	1.1	—	(0.9)	—
Tax (expense)/benefit	(0.4)	—	0.4	—
Unrealized gains/(losses) on cash flow hedging instruments	8.1	(3.8)	19.9	(20.7)
Tax (expense)/benefit	(2.1)	(0.1)	(6.0)	0.3
Unrealized gains/(losses) on net investment hedging instruments	(3.9)	11.7	5.9	26.4
Tax (expense)/benefit	1.4	(4.3)	(2.2)	(9.7)
Reclassification adjustment for net (gains)/losses realized in net earnings for cash flow hedges and available-for-sale securities	(2.2)	10.3	5.4	16.1
Tax expense/(benefit)	1.0	(0.8)	0.9	(1.4)
Translation adjustment	7.7	(35.7)	(22.7)	(49.7)
Tax (expense)/benefit	(15.1)	(6.5)	(3.4)	(1.3)
Other comprehensive income/(loss)	(4.4)	(29.2)	(2.7)	(40.0)
Comprehensive income including noncontrolling interests	422.5	361.5	964.9	783.1
Comprehensive income/(loss) attributable to noncontrolling interests	(0.1)	0.3	—	0.6
Comprehensive income attributable to Starbucks	$422.6	$361.2	$964.9	$782.5

See Notes to Condensed Consolidated Financial Statements

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STARBUCKS CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS
(in millions, except per share data)
(unaudited)

	Mar 30, 2014	Sep 29, 2013
ASSETS		
Current assets:		
Cash and cash equivalents	$1,190.3	$2,575.7
Short-term investments	299.2	658.1
Accounts receivable, net	590.0	561.4
Inventories	954.7	1,111.2
Prepaid expenses and other current assets	286.1	287.7
Deferred income taxes, net	258.7	277.3
Total current assets	3,579.0	5,471.4
Long-term investments	449.8	58.3
Equity and cost investments	512.8	496.5
Property, plant and equipment, net	3,278.1	3,200.5
Deferred income taxes, net	943.4	967.0
Other assets	195.9	185.3
Other intangible assets	277.2	274.8
Goodwill	860.8	862.9
TOTAL ASSETS	$10,097.0	$11,516.7
LIABILITIES AND EQUITY		
Current liabilities:		
Accounts payable	$472.6	$491.7
Accrued litigation charge	—	2,784.1
Accrued liabilities	1,260.1	1,269.3
Insurance reserves	184.5	178.5
Deferred revenue	816.3	653.7
Total current liabilities	2,733.5	5,377.3
Long-term debt	2,048.0	1,299.4
Other long-term liabilities	368.4	357.7
Total liabilities	5,149.9	7,034.4
Shareholders' equity:		
Common stock ($0.001 par value) — authorized, 1,200.0 shares; issued and outstanding, 754.1 shares and 753.2 shares, respectively	0.8	0.8
Additional paid-in capital	174.6	282.1
Retained earnings	4,705.4	4,130.3
Accumulated other comprehensive income	64.3	67.0
Total shareholders' equity	4,945.1	4,480.2
Noncontrolling interest	2.0	2.1
Total equity	4,947.1	4,482.3
TOTAL LIABILITIES AND EQUITY	$10,097.0	$11,516.7

See Notes to Condensed Consolidated Financial Statements

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STARBUCKS CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(in millions, unaudited)

	Two Quarters Ended	
	Mar 30, 2014	Mar 31, 2013
OPERATING ACTIVITIES:		
Net earnings including noncontrolling interests	$967.6	$823.1
Adjustments to reconcile net earnings to net cash (used)/provided by operating activities:		
Depreciation and amortization	364.2	318.1
Deferred income taxes, net	36.1	(6.9)
Income earned from equity method investees, net of distributions	(20.8)	(15.9)
Gain resulting from sale of equity in joint venture	—	(35.2)
Stock-based compensation	91.6	70.9
Other	11.4	11.2
Cash (used)/provided by changes in operating assets and liabilities:		
Accounts receivable	(28.6)	(25.2)
Inventories	156.2	138.6
Accounts payable	(9.6)	(37.2)
Accrued litigation charge	(2,763.9)	—
Accrued liabilities and insurance reserves	54.2	(36.9)
Deferred revenue	162.5	154.0
Prepaid expenses, other current assets and other assets	(4.4)	13.9
Net cash (used)/provided by operating activities	(983.5)	1,372.5
INVESTING ACTIVITIES:		
Purchase of investments	(974.9)	(119.9)
Sales, maturities and calls of investments	943.9	569.9
Acquisitions, net of cash acquired	—	(568.8)
Additions to property, plant and equipment	(503.6)	(484.9)
Other	(14.4)	(9.3)
Net cash used by investing activities	(549.0)	(613.0)
FINANCING ACTIVITIES:		
Proceeds from issuance of long-term debt	748.5	—
Principal payments on long-term debt	—	(35.2)
Proceeds from issuance of common stock	89.5	141.0
Excess tax benefit on share-based awards	87.3	193.2
Cash dividends paid	(392.3)	(313.5)
Repurchase of common stock	(290.1)	(588.1)
Minimum tax withholdings on share-based awards	(76.0)	(119.9)
Other	(9.5)	4.0
Net cash provided/(used) by financing activities	157.4	(718.5)
Effect of exchange rate changes on cash and cash equivalents	(10.3)	(6.4)
Net (decrease)/increase in cash and cash equivalents	(1,385.4)	34.6
CASH AND CASH EQUIVALENTS:		
Beginning of period	2,575.7	1,188.6
End of period	$1,190.3	$1,223.2
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Cash paid during the period for:		

Interest, net of capitalized interest	$17.4	$17.2
Income taxes	$314.8	$238.1

See Notes to Condensed Consolidated Financial Statements

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STARBUCKS CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

Note 1: Summary of Significant Accounting Policies

Financial Statement Preparation

The unaudited condensed consolidated financial statements as of March 30, 2014, and for the quarter and two quarters ended March 30, 2014 and March 31, 2013, have been prepared by Starbucks Corporation under the rules and regulations of the Securities and Exchange Commission ("SEC"). In the opinion of management, the financial information for the quarter and two quarters ended March 30, 2014 and March 31, 2013 reflects all adjustments and accruals, which are of a normal recurring nature, necessary for a fair presentation of the financial position, results of operations and cash flows for the interim periods. In this Quarterly Report on Form 10-Q ("10-Q") Starbucks Corporation is referred to as "Starbucks," the "Company," "we," "us" or "our."

The financial information as of September 29, 2013 is derived from our audited consolidated financial statements and notes for the fiscal year ended September 29, 2013 ("fiscal 2013") included in Item 8 in the Fiscal 2013 Annual Report on Form 10-K (the "10-K"). The information included in this 10-Q should be read in conjunction with the footnotes and management's discussion and analysis of the financial statements in the 10-K.

The results of operations for the quarter and two quarters ended March 30, 2014 are not necessarily indicative of the results of operations that may be achieved for the entire fiscal year ending September 28, 2014 ("fiscal 2014").

Recent Accounting Pronouncements

In July 2013, the Financial Accounting Standards Board ("FASB") issued guidance on the financial statement presentation of an unrecognized tax benefit when a net operating loss carryforward, a similar tax loss, or a tax credit carryforward exists. This guidance requires the unrecognized tax benefit to be presented in the financial statements as a reduction to a deferred tax asset. When a deferred tax asset is not available, or the asset is not intended to be used for this purpose, the unrecognized tax benefit should be presented in the financial statements as a liability and not netted with a deferred tax asset. The guidance will become effective for us at the beginning of our first quarter of fiscal 2015. We do not expect the adoption of this guidance will have a material impact on our financial statements.

In March 2013, the FASB issued guidance on a parent's accounting for the cumulative translation adjustment upon derecognition of certain subsidiaries or groups of assets within a foreign entity or of an investment in a foreign entity. This guidance requires a parent to release any related cumulative translation adjustment into net income only if the sale or transfer results in the complete or substantially complete liquidation of the foreign entity in which the subsidiary or group of assets had resided. The guidance will become effective for us at the beginning of our first quarter of fiscal 2015. We do not expect the adoption of this guidance will have a material impact on our financial statements.

In February 2013, the FASB issued guidance that adds additional disclosure requirements for items reclassified out of accumulated other comprehensive income. This guidance requires the disclosure of significant amounts reclassified from each component of accumulated other comprehensive income and the income statement line items affected by the reclassification. The guidance became effective for us at the beginning of our first quarter of fiscal 2014 and the additional disclosures are provided in Note 7 of this 10-Q.

In January 2013, the FASB issued guidance clarifying the scope of disclosure requirements for offsetting assets and liabilities. The amended guidance limits the scope of balance sheet offsetting disclosures to derivatives, repurchase agreements, and securities lending transactions to the extent that they are offset in the financial statements or subject to an enforceable master netting arrangement or similar agreement. The guidance became effective for us at the beginning of our first quarter of fiscal 2014 and did not have a material impact on our financial statements.

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Correction of an Immaterial Error

Effective at the beginning of fiscal 2014, we reclassified certain fees related to our US and Seattle's Best Coffee foodservice operations in our Channel Development segment and All Other Segments, respectively, from other operating expenses to foodservice revenues included in CPG, foodservice and other net revenues in our consolidated statements of earnings. This reclassification results from a correction of an error in our prior period financial statements which we have determined to be immaterial. In order to align prior period classifications with the current period presentation, the historical consolidated financial statements have been corrected, resulting in reclassifications of $25.4 million and $22.7 million for fiscal years 2013 and 2012, respectively. The reclassifications for the quarter and two quarters ended March 31, 2013 were $6.3 million and $12.7 million, respectively. The consolidated statements of earnings as corrected are presented below (in millions):

	Fiscal 2013					Fiscal 2012
	Q1	Q2	Q3	Q4	Full Year	Full Year
Net revenues						
Company-operated stores	$2,989.6	$2,807.7	$2,986.3	$3,009.6	$11,793.2	$10,534.5
Licensed stores	350.2	322.1	342.0	346.3	1,360.5	1,210.3
CPG, foodservice and other	453.4	419.8	407.0	432.9	1,713.1	1,532.0
Total net revenues	3,793.2	3,549.6	3,735.3	3,788.8	14,866.8	13,276.8
Cost of sales including occupancy costs	1,620.7	1,530.4	1,597.6	1,633.7	6,382.3	5,813.3
Store operating expenses	1,089.5	1,038.4	1,084.1	1,073.9	4,286.1	3,918.1
Other operating expenses	126.1	105.8	98.9	101.1	431.8	407.2
Depreciation and amortization expenses	148.9	153.1	153.3	166.1	621.4	550.3
General and administrative expenses	231.9	230.3	249.6	226.1	937.9	801.2
Litigation charge	—	—	—	2,784.1	2,784.1	—
Total operating expenses	3,217.1	3,058.0	3,183.5	5,985.0	15,443.6	11,490.1
Income from equity investees	54.5	52.5	63.4	81.0	251.4	210.7
Operating income/(loss)	630.6	544.1	615.2	(2,115.2)	(325.4)	1,997.4
Interest income and other, net	(2.9)	50.8	3.5	72.1	123.6	94.4
Interest expense	(6.6)	(6.1)	(6.3)	(9.1)	(28.1)	(32.7)
Earnings/(loss) before income taxes	621.1	588.8	612.4	(2,052.2)	(229.9)	2,059.1
Income taxes	188.7	198.1	194.6	(820.1)	(238.7)	674.4
Net earnings including noncontrolling interests	432.4	390.7	417.8	(1,232.1)	8.8	1,384.7
Net earnings attributable to noncontrolling interests	0.2	0.3	—	(0.1)	0.5	0.9
Net earnings attributable to Starbucks	$432.2	$390.4	$417.8	$(1,232.0)	$8.3	$1,383.8

There was no impact on operating income or net earnings as a result of the error correction, nor any impact on our consolidated statements of comprehensive income, consolidated balance sheets or consolidated statements of cash flows. Additional disclosure regarding this change as it relates to our segment results is included at Note 11, Segment Reporting.

Note 2: Derivative Financial Instruments

Interest Rates

Depending on market conditions, we enter into interest rate swap agreements to hedge the variability in cash flows due to changes in the benchmark interest rate related to anticipated debt issuances. These agreements are cash settled at the time of the pricing of the related debt. The effective portion of the derivative's gain or loss is recorded in accumulated other comprehensive income ("AOCI") and is subsequently reclassified to interest expense over the life of the related debt.

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Foreign Currency

To reduce cash flow volatility from foreign currency fluctuations, we enter into forward and swap contracts to hedge portions of cash flows of anticipated revenue streams and inventory purchases in currencies other than the entity's functional currency. The effective portion of the derivative's gain or loss is recorded in AOCI and is subsequently reclassified to revenue or cost of sales when the hedged exposure affects net earnings.

We also enter into forward contracts to hedge the foreign currency exposure of our net investment in certain of our equity method investees. The effective portion of the derivative's gain or loss is recorded in AOCI and will be subsequently reclassified to net earnings when the hedged net investment is either sold or substantially liquidated.

To mitigate the translation risk of certain balance sheet items, we enter into foreign currency swap contracts that are not designated as hedging instruments. Gains and losses from these derivatives are largely offset by the financial impact of translating foreign currency denominated payables and receivables; both are recorded in net interest income and other.

Commodities

Depending on market conditions, we enter into coffee futures contracts and collars (the combination of a purchased call option and a sold put option) to hedge a portion of anticipated cash flows under our price-to-be-fixed green coffee contracts, which are described further in Note 4, Inventories. The effective portion of the derivative's gain or loss is recorded in AOCI and is subsequently reclassified to cost of sales when the hedged exposure affects net earnings.

To mitigate the price uncertainty of a portion of our future purchases of dairy products and diesel fuel, we enter into dairy futures and collars, as well as diesel fuel swap contracts that are not designated as hedging instruments. Gains and losses from these derivatives are recorded in net interest income and other. Gains and losses from dairy futures largely offset price fluctuations on our dairy purchases, which are included in cost of sales. Gains and losses from diesel fuel swaps largely offset the financial impact of diesel fuel fluctuations on our shipping costs, which are included in operating expenses.

Gains and losses on derivative contracts designated as hedging instruments included in AOCI and expected to be reclassified into earnings within 12 months, net of tax (in millions):

	Net Gains/(Losses) Included in AOCI		Net Gains/(Losses) Expected to be Reclassified from AOCI into Earnings within 12 Months	Contract Remaining Maturity (Months)
	Mar 30, 2014	Sep 29, 2013		
Cash Flow Hedges:				
Interest rates	$38.0	$41.4	$3.2	
Foreign currency	10.3	(0.3)	6.0	34
Coffee	(1.5)	(12.2)	(1.9)	17
Net Investment Hedges:				
Foreign currency	(9.2)	(12.9)		36

Pretax gains and losses on derivative contracts designated as hedging instruments recognized in other comprehensive income ("OCI") and reclassifications from AOCI to earnings (in millions)

	Quarter Ended				Two Quarters Ended			
	Gains/(Losses) Recognized in OCI Before Reclassifications		Gains/(Losses) Reclassified from AOCI to Earnings		Gains/(Losses) Recognized in OCI Before Reclassifications		Gains/(Losses) Reclassified from AOCI to Earnings	
	Mar 30, 2014	Mar 31, 2013	Mar 30, 2014	Mar 31, 2013	Mar 30, 2014	Mar 31, 2013	Mar 30, 2014	Mar 31, 2013
Cash Flow Hedges:								
Interest rates	$—	$—	$1.3	$—	$0.5	$—	$2.5	$—

Foreign currency	7.0	1.8	2.1	1.2	18.6	6.4	3.3	0.6
Coffee	1.1	(5.6)	(0.9)	(11.1)	0.8	(27.1)	(10.9)	(16.3)
Net Investment Hedges:								
Foreign currency	(3.9)	11.7	—	—	5.9	26.4	—	—

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Pretax gains and losses on derivative contracts not designated as hedging instruments recognized in earnings (in millions):

	Gains/(Losses) Recognized in Earnings			
	Quarter Ended		Two Quarters Ended	
	Mar 30, 2014	Mar 31, 2013	Mar 30, 2014	Mar 31, 2013
Foreign currency	$(0.1)	$3.3	$(1.0)	$2.2
Coffee	—	0.6	—	(2.1)
Dairy	7.4	(1.1)	11.9	(2.6)
Diesel fuel	—	0.1	—	0.1

Notional amounts of outstanding derivative contracts (in millions):

	Mar 30, 2014	Sep 29, 2013
Foreign currency	$512	$452
Coffee	37	—
Dairy	21	38
Diesel fuel	18	17

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Note 3: Fair Value Measurements
Assets and Liabilities Measured at Fair Value on a Recurring Basis (in millions):

	Balance at Mar 30, 2014	Fair Value Measurements at Reporting Date Using		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Cash and cash equivalents	$1,190.3	$ 1,190.3	$ —	$ —
Short-term investments:				
Available-for-sale securities				
Commercial paper	4.0	—	4.0	—
Corporate debt securities	16.3	—	16.3	—
Foreign government obligations	6.4	—	6.4	—
US government treasury securities	44.0	44.0	—	—
State and local government obligations	14.4	—	14.4	—
Short-term bond funds	80.1	80.1	—	—
Certificates of deposit	63.8	—	63.8	—
Total available-for-sale securities	229.0	124.1	104.9	—
Trading securities	70.2	70.2	—	—
Total short-term investments	299.2	194.3	104.9	—
Prepaid expenses and other current assets:				
Derivative assets	27.7	5.2	22.5	—
Long-term investments:				
Available-for-sale securities				
Agency obligations	9.2	—	9.2	—
Corporate debt securities	196.8	—	196.8	—
Auction rate securities	13.5	—	—	13.5
Foreign government obligations	4.0	—	4.0	—
US government treasury securities	148.9	148.9	—	—
State and local government obligations	6.9	—	6.9	—
Mortgage and asset-backed securities	70.5	—	70.5	—
Total long-term investments	449.8	148.9	287.4	13.5
Other assets:				
Derivative assets	11.8	—	11.8	—
Total	$1,978.8	$ 1,538.7	$ 426.6	$ 13.5
Liabilities:				
Accrued liabilities:				
Derivative liabilities	$0.4	$ 0.2	$ 0.2	$ —
Other long-term liabilities:				
Derivative liabilities	0.2	—	0.2	—
Total	$0.6	$ 0.2	$ 0.4	$ —

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	Balance at Sep 29, 2013	Fair Value Measurements at Reporting Date Using Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Cash and cash equivalents	$2,575.7	$ 2,575.7	$ —	$ —
Short-term investments:				
Available-for-sale securities				
Agency obligations	20.0	—	20.0	—
Commercial paper	127.0	—	127.0	—
Corporate debt securities	57.5	—	57.5	—
Government treasury securities	352.9	352.9	—	—
Certificates of deposit	34.1	—	34.1	—
Total available-for-sale securities	591.5	352.9	238.6	—
Trading securities	66.6	66.6	—	—
Total short-term investments	658.1	419.5	238.6	—
Prepaid expenses and other current assets:				
Derivative assets	12.5	—	12.5	—
Long-term investments:				
Available-for-sale securities				
Agency obligations	8.1	—	8.1	—
Corporate debt securities	36.8	—	36.8	—
Auction rate securities	13.4	—	—	13.4
Total long-term investments	58.3	—	44.9	13.4
Other assets:				
Derivative assets	11.4	—	11.4	—
Total	$3,316.0	$ 2,995.2	$ 307.4	$ 13.4
Liabilities:				
Accrued liabilities:				
Derivative liabilities	$3.5	$ —	$ 3.5	$ —
Other long-term liabilities:				
Derivative liabilities	0.5	—	0.5	—
Total	$4.0	$ —	$ 4.0	$ —

There were no material transfers between levels and there was no significant activity within Level 3 instruments during the periods presented. In the second quarter of fiscal 2014, we revised the classification of coffee and dairy futures from Level 2 to Level 1, as we use quoted prices in active markets for identical assets to determine fair value. The fair values of any financial instruments presented above exclude the impact of netting assets and liabilities when a legally enforceable master netting agreement exists.

Gross unrealized holding gains and losses on investments were not material as of March 30, 2014 and September 29, 2013.

Assets and Liabilities Measured at Fair Value on a Nonrecurring Basis

Assets and liabilities recognized or disclosed at fair value in the financial statements on a nonrecurring basis include items such as property, plant and equipment, goodwill and other intangible assets, equity and cost method investments, and other assets. These assets are measured at fair value if determined to be impaired. During the the quarter and two quarters ended March 30, 2014 and March 31, 2013, there were no material fair value adjustments. The estimated fair value of our long-term debt based on the quoted market price (Level 2) is included at Note 6, Debt.

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Note 4: Inventories

(in millions)	Mar 30, 2014	Sep 29, 2013	Mar 31, 2013
Coffee:			
Unroasted	$400.0	$493.0	$590.4
Roasted	189.5	235.4	214.3
Other merchandise held for sale	210.1	243.3	200.7
Packaging and other supplies	155.1	139.5	119.1
Total	$954.7	$1,111.2	$1,124.5

Other merchandise held for sale includes, among other items, tea and serveware. Inventory levels vary due to seasonality, commodity market supply and price fluctuations.

As of March 30, 2014, we had committed to purchasing green coffee totaling $534 million under fixed-price contracts and an estimated $560 million under price-to-be-fixed contracts. As of March 30, 2014, approximately $33 million of our price-to-be-fixed contracts were effectively fixed through the use of futures contracts and approximately $4 million were price-protected through the use of collar instruments. Price-to-be-fixed contracts are purchase commitments whereby the quality, quantity, delivery period, and other negotiated terms are agreed upon, but the date, and therefore the price, at which the base “C” coffee commodity price component will be fixed has not yet been established. For these types of contracts, either Starbucks or the seller has the option to “fix” the base “C” coffee commodity price prior to the delivery date. Until prices are fixed, we estimate the total cost of these purchase commitments. We believe, based on relationships established with our suppliers in the past, the risk of non-delivery on these purchase commitments is remote.

Note 5: Supplemental Balance Sheet Information (in millions)

Property, Plant and Equipment, net	Mar 30, 2014	Sep 29, 2013
Land	$46.9	$47.0
Buildings	277.9	259.6
Leasehold improvements	4,611.1	4,431.6
Store equipment	1,412.3	1,353.9
Roasting equipment	415.4	397.9
Furniture, fixtures and other	1,007.8	949.7
Work in progress	347.3	342.4
Property, plant and equipment, gross	8,118.7	7,782.1
Less accumulated depreciation	(4,840.6)	(4,581.6)
Property, plant and equipment, net	$3,278.1	$3,200.5

Accrued Liabilities	Mar 30, 2014	Sep 29, 2013
Accrued compensation and related costs	$379.1	$420.2
Accrued occupancy costs	114.6	120.7
Accrued taxes	133.6	125.0
Accrued dividend payable	196.1	195.8
Other	436.7	407.6
Total accrued liabilities	$1,260.1	$1,269.3

Note 6: Debt

In December 2013, we issued $400 million of 3-year 0.875% Senior Notes ("the 2014 3-year notes") due December 2016, and $350 million of 5-year 2.000% Senior Notes ("the 2014 5-year notes") due December 2018, in an underwritten registered public offering. Interest on both of these notes is payable semi-annually on June 5 and December 5 of each year, commencing on June 5, 2014.

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Components of long-term debt including the associated interest rates and related fair values (in millions, except interest rates):

		Mar 30, 2014		Sep 29, 2013			
Issuance	Due Date	Face Value	Estimated Fair Value	Face Value	Estimated Fair Value	Stated Interest Rate	Effective Interest Rate [1]
2014 3-year notes	December 2016	$400.0	$400.0	$—	$—	0.875 %	0.941 %
2007 notes	August 2017	550.0	636.0	550.0	644.0	6.250 %	6.292 %
2014 5-year notes	December 2018	350.0	349.0	—	—	2.000 %	2.012 %
2013 notes	October 2023	750.0	770.0	750.0	762.0	3.850 %	2.860 %
Total		2,050.0	2,155.0	1,300.0	1,406.0		
Aggregate unamortized discount		2.0		0.6			
Total		$2,048.0		$1,299.4			

(1) Includes the effects of the amortization of any premium or discount and any gain or loss upon settlement of related treasury locks or forward-starting interest rate swaps utilized to hedge the interest rate risk prior to the debt issuance.

The indentures under which the above notes were issued also require us to maintain compliance with certain covenants, including limits on future liens and sale and leaseback transactions on certain material properties. As of March 30, 2014, we were in compliance with all applicable covenants.

Note 7: Equity

Changes in total equity (in millions):

	Two Quarters Ended	
	Mar 30, 2014	Mar 31, 2013
Beginning balance of total equity	$4,482.3	$5,114.5
Net earnings including noncontrolling interests	967.6	823.1
Other comprehensive income/(loss)	(2.7)	(40.0)
Stock-based compensation expense	92.6	71.9
Exercise of stock options/vesting of RSUs	90.0	205.2
Sale of common stock	11.0	10.2
Repurchase of common stock	(301.2)	(544.1)
Cash dividends declared	(392.5)	(313.3)
Ending balance of total equity	$4,947.1	$5,327.5

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Changes in accumulated other comprehensive income ("AOCI") by component, for the quarter and two quarters ended March 30, 2014, net of tax:

Quarter Ended

(in millions)	Available-for-Sale Securities	Cash Flow Hedges	Net Investment Hedges	Translation Adjustment	Total
Net gains/(losses) in AOCI at December 29, 2013	$ (1.7)	$42.2	$(6.7)	$34.9	$68.7
Net gains/(losses) recognized in OCI before reclassifications	0.7	6.0	(2.5)	(7.4)	(3.2)
Net (gains)/losses reclassified from AOCI to earnings	0.2	(1.4)	—	—	(1.2)
Other comprehensive income/(loss)	0.9	4.6	(2.5)	(7.4)	(4.4)
Net gains/(losses) in AOCI at March 30, 2014	$ (0.8)	$46.8	$(9.2)	$27.5	$64.3

Two Quarters Ended

(in millions)	Available-for-Sale Securities	Cash Flow Hedges	Net Investment Hedges	Translation Adjustment	Total
Net gains/(losses) in AOCI at September 29, 2013	$ (0.5)	$26.8	$(12.9)	$53.6	$67.0
Net gains/(losses) recognized in OCI before reclassifications	(0.5)	13.9	3.7	(26.1)	(9.0)
Net (gains)/losses reclassified from AOCI to earnings	0.2	6.1	—	—	6.3
Other comprehensive income/(loss)	(0.3)	20.0	3.7	(26.1)	(2.7)
Net gains/(losses) in AOCI at March 30, 2014	$ (0.8)	$46.8	$(9.2)	$27.5	$64.3

Impact of reclassifications from AOCI on the consolidated statements of earnings related to cash flow hedges for the quarter and two quarters ended March 30, 2014:

Quarter Ended

AOCI Components	Amounts Reclassified from AOCI (in millions)	Affected Line Item in the Statements of Earnings
Gains/(losses) on cash flow hedges		
Interest rate hedges	$1.3	Interest expense
Foreign currency hedges	1.3	Revenue
Foreign currency/coffee hedges	(0.1)	Cost of sales including occupancy costs
	2.5	Total before tax
	(1.1)	Tax (expense)/benefit
	$1.4	Net of tax

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Two Quarters Ended

AOCI Components	Amounts Reclassified from AOCI (in millions)		Affected Line Item in the Statements of Earnings
Gains/(losses) on cash flow hedges			
Interest rate hedges	$2.5		Interest expense
Foreign currency hedges	2.3		Revenue
Foreign currency / coffee hedges	(9.9	)	Cost of sales including occupancy costs
	(5.1	)	Total before tax
	(1.0	)	Tax (expense)/benefit
	$(6.1	)	Net of tax

In addition to 1.2 billion shares of authorized common stock with $0.001 par value per share, the Company has authorized 7.5 million shares of preferred stock, none of which was outstanding as of March 30, 2014.
We repurchased 4.1 million shares of common stock at a total cost of $301.2 million, and 10.8 million shares at a total cost of $544.1 million for the two quarters ended March 30, 2014 and March 31, 2013, respectively. As of March 30, 2014, 22.3 million shares remained available for repurchase under current authorizations.

During the second quarter of fiscal 2014, our Board of Directors declared a quarterly cash dividend to shareholders of $0.26 per share to be paid on May 23, 2014 to shareholders of record as of the close of business on May 8, 2014.

Note 8: Employee Stock Plans

As of March 30, 2014, there were 56.2 million shares of common stock available for issuance pursuant to future equity-based compensation awards and 7.6 million shares available for issuance under our employee stock purchase plan.

Stock-based compensation expense recognized in the consolidated statements of earnings (in millions):

	Quarter Ended		Two Quarters Ended	
	Mar 30, 2014	Mar 31, 2013	Mar 30, 2014	Mar 31, 2013
Options	$9.7	$7.9	$22.5	$19.8
Restricted Stock Units (“RSUs”)	34.1	25.6	69.1	51.1
Total stock-based compensation	$43.8	$33.5	$91.6	$70.9

Stock option and RSU transactions from September 29, 2013 through March 30, 2014 (in millions):

	Stock Options		RSUs	
Options outstanding/Nonvested RSUs, September 29, 2013	22.0		5.8	
Granted	3.0		2.4	
Options exercised/RSUs vested	(3.2	)	(2.5	)
Forfeited/expired	(0.3	)	(0.4	)
Options outstanding/Nonvested RSUs, March 30, 2014	21.5		5.3	
Total unrecognized stock-based compensation expense, net of estimated forfeitures, as of March 30, 2014	$51.9		$153.0	

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Note 9: Earnings Per Share

Calculation of net earnings per common share (“EPS”) — basic and diluted (in millions, except EPS):

	Quarter Ended		Two Quarters Ended	
	Mar 30, 2014	Mar 31, 2013	Mar 30, 2014	Mar 31, 2013
Net earnings attributable to Starbucks	$427.0	$390.4	$967.6	$822.5
Weighted average common shares outstanding (for basic calculation)	755.2	749.1	755.0	747.6
Dilutive effect of outstanding common stock options and RSUs	9.4	12.2	10.4	13.7
Weighted average common and common equivalent shares outstanding (for diluted calculation)	764.6	761.3	765.4	761.3
EPS — basic	$0.57	$0.52	$1.28	$1.10
EPS — diluted	$0.56	$0.51	$1.26	$1.08

Potential dilutive shares consist of the incremental common shares issuable upon the exercise of outstanding stock options (both vested and non-vested) and unvested RSUs, calculated using the treasury stock method. The calculation of dilutive shares outstanding excludes out-of-the-money stock options (i.e., such options’ exercise prices were greater than the average market price of our common shares for the period) because their inclusion would have been antidilutive. Out-of-the-money stock options totaled approximately 2.8 million and less than 0.1 million as of March 30, 2014 and March 31, 2013, respectively.

Note 10: Commitments and Contingencies

Legal Proceedings

On November 12, 2013, the arbitrator in our arbitration with Kraft Foods Global, Inc. (now known as Kraft Foods Group, Inc.) (“Kraft”) ordered Starbucks to pay Kraft $2,227.5 million in damages plus prejudgment interest and attorneys' fees. We estimated prejudgment interest, which included an accrual through the estimated payment date, and attorneys' fees to be approximately $556.6 million. As a result, we recorded a litigation charge of $2,784.1 million in our fiscal 2013 operating results.

In the first quarter of fiscal 2014, Starbucks paid all amounts due to Kraft under the arbitration, including prejudgment interest and attorneys' fees, and fully extinguished the litigation charge liability. Of the $2,784.1 million litigation charge accrued in the fourth quarter of fiscal 2013, $2,763.9 million was paid and the remainder was released as a litigation credit to reflect a reduction to our estimated prejudgment interest payable as a result of paying our obligation earlier than anticipated.

Starbucks is party to various other legal proceedings arising in the ordinary course of business, including, at times, certain employment litigation cases that have been certified as class or collective actions, but is not currently a party to any legal proceeding that management believes could have a material adverse effect on our consolidated financial position, results of operations or cash flows.

Note 11: Segment Reporting

Segment information is prepared on the same basis that our ceo, who is our chief operating decision maker, manages the segments, evaluates financial results, and makes key operating decisions.

The table below presents financial information for our reportable operating segments and All Other Segments for the quarter and two quarters ended March 30, 2014 and March 31, 2013, including reclassifications resulting from the correction of the immaterial error discussed in Note 1. The reclassifications for fiscal years 2013 and 2012 were $21.8 million and $19.2 million for the Channel Development segment, respectively, and $3.6 million and $3.5 million for All Other Segments, respectively. The reclassifications for the quarter and two quarters ended March 31, 2013 were $5.4 million and $10.9 million for the Channel Development segment, respectively, and $0.9 million and $1.8 million for All Other Segments, respectively.

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Quarter Ended (in millions)	Americas	EMEA	China / Asia Pacific	Channel Development	All Other Segments	Segment Total
March 30, 2014						
Total net revenues	$2,808.8	$309.9	$265.3	$ 370.4	$119.4	$3,873.8
Depreciation and amortization expenses	114.8	14.8	11.8	0.4	3.7	145.5
Income from equity investees	—	1.1	37.4	21.4	—	59.9
Operating income/(loss)	605.6	17.7	87.0	127.3	(7.8)	829.8
March 31, 2013						
Total net revenues	$2,604.1	$273.2	$213.6	$ 338.1	$120.6	$3,549.6
Depreciation and amortization expenses	105.6	13.7	8.5	0.3	3.4	131.5
Income from equity investees	2.4	—	30.8	19.3	—	52.5
Operating income/(loss)	549.7	5.2	68.3	94.1	(4.1)	713.2

Two Quarters Ended (in millions)	Americas	EMEA	China / Asia Pacific	Channel Development	All Other Segments	Segment Total
March 30, 2014						
Total net revenues	$5,881.7	$649.5	$532.2	$ 771.5	$278.5	$8,113.4
Depreciation and amortization expenses	227.1	29.4	22.0	0.8	7.3	286.6
Income from equity investees	—	1.9	70.5	38.6	—	111.0
Operating income	1,337.6	51.2	168.0	246.2	6.1	1,809.1
March 31, 2013						
Total net revenues	$5,444.7	$579.3	$427.7	$ 712.5	$178.5	$7,342.7
Depreciation and amortization expenses	211.0	27.9	15.9	0.6	4.3	259.7
Income from equity investees	2.4	—	64.9	39.7	—	107.0
Operating income/(loss)	1,139.8	27.5	140.4	191.0	(8.2)	1,490.5

Reconciliation of total segment operating income to consolidated earnings before income taxes (in millions):

	Quarter Ended		Two Quarters Ended	
	Mar 30, 2014	Mar 31, 2013	Mar 30, 2014	Mar 31, 2013
Total segment operating income	$829.8	$713.2	$1,809.1	$1,490.5
Unallocated corporate operating expenses	(185.7)	(169.1)	(351.4)	(315.9)
Consolidated operating income	644.1	544.1	1,457.7	1,174.6
Interest income and other, net	17.8	50.8	37.6	48.0
Interest expense	(16.7)	(6.1)	(31.3)	(12.7)
Earnings before income taxes	$645.2	$588.8	$1,464.0	$1,209.9

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

CAUTIONARY STATEMENT PURSUANT TO THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995

Certain statements herein, including statements regarding trends in or expectations relating to the expected effects of our initiatives and plans, as well as trends in or expectations regarding earnings per share, revenues, operating income, operating margins, comparable store sales, sales leverage, sales growth, profitability, expenses, dividends, share repurchases, other financial results, capital expenditures, scaling and expansion of international operations, shifts in our store portfolio to more licensed stores in EMEA and to more company-operated stores in CAP, profitable growth models and opportunities, strategic acquisitions, commodity costs and our mitigation strategies, the transition from our distribution arrangement with Kraft to a direct distribution model, liquidity, cash flow from operations, use of cash, the potential issuance of debt and applicable interest rate, anticipated store openings, closings and renovations, the health and growth of our business overall and of specific businesses or markets, benefits of recent initiatives, increased traffic to our stores, operational efficiencies, product innovation and distribution, tax rates, and economic conditions in the US and international markets, constitute "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. Such statements are based on currently available operating, financial and competitive information and are subject to various risks and uncertainties. Actual future results and trends may differ materially depending on a variety of factors, including, but not limited to, coffee, dairy and other raw materials prices and availability, successful execution of our initiatives, successful execution of internal plans, fluctuations in US and international economies and currencies, the impact of competitors' initiatives, the effect of legal proceedings, and other risks detailed in our filings with the SEC, including in Part I Item IA "Risk Factors" in the 10-K.

A forward-looking statement is neither a prediction nor a guarantee of future events or circumstances, and those future events or circumstances may not occur. You should not place undue reliance on the forward-looking statements, which speak only as of the date of this report. We are under no obligation to update or alter any forward-looking statements, whether as a result of new information, future events or otherwise.

This information should be read in conjunction with the condensed consolidated financial statements and the notes included in Item 1 of Part I of this 10-Q and the audited consolidated financial statements and notes, and Management's Discussion and Analysis of Financial Condition and Results of Operations, contained in the 10-K.

General

Our fiscal year ends on the Sunday closest to September 30. All references to store counts, including data for new store openings, are reported net of store closures, unless otherwise noted.

Overview

Starbucks second quarter results reflect improvements across all segments. Consolidated total net revenues increased 9% to $3.9 billion, driven by global comparable store sales growth of 6%. Consolidated operating income increased $100 million, or 18%, to $644 million. Operating margin expanded across all reportable segments, contributing to a consolidated operating margin of 16.6%, reflecting growth of 130 basis points over the prior year quarter. Earnings per share of $0.56 increased 10% over the prior year quarter earnings per share of $0.51, which included a $0.03 per share gain on the sale of our equity interest in our Mexico joint venture operations.

The Americas segment continued its solid performance in the second quarter, growing revenues by 8% to $2.8 billion, primarily driven by comparable store sales growth of 6%, comprised of a 3% increase in average ticket and a 2% increase in number of transactions. Successful promotional beverages and expanded food offerings, including the rollout of our La Boulange™ food platform in the US, contributed to the growth in comparable store sales. Operating margin expanded 50 basis points to 21.6%, primarily due to lower commodity costs, mainly coffee. Looking forward, we expect to continue to drive revenue growth and margin expansion through new stores and expanded product offerings. We plan to continue elevating our food program, in part with the completion of the rollout of La Boulange™ bakery items in our US stores and enhancements to our lunch options.

In the EMEA segment, the combination of solid company-operated and licensed store growth drove increased revenues and profitability. Revenues grew 13% to $310 million, driven by favorable foreign currency exchange and comparable store sales growth of 6%, the highest growth in the region in fourteen quarters. Incremental revenues from 168 net new licensed store openings over the past year also contributed. Sales leverage, largely driven by our strategic

portfolio shift to higher margin licensed stores, and continued cost management drove the increase in operating margin of 380 basis points over the prior year quarter, to 5.7%. We expect continued disciplined licensed store expansion and a focus on the customer experience in this region will result in improved operating performance as we progress on our plan towards mid-teens operating margin over time.

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The China/Asia Pacific segment leveraged strong sales in the quarter to offset the unfavorable margin impact of the portfolio shift toward more company-operated stores in this segment. New store growth, along with a 7% increase in comparable store sales, drove a 24% increase in revenues to $265 million. The 7% growth in comparable store sales was driven by an increase in number of transactions. Operating income grew 27% to $87 million, while operating margin expanded 80 basis points to 32.8%, primarily driven by sales leverage. We expect this segment will become a more meaningful contributor to overall company profitability in the future, as we look forward to continued new store openings and establishing China as our largest market outside of the US.

Channel Development segment revenues grew 10% for the quarter to $370 million, primarily due to increased sales of premium single serve products, driven by sales of Starbucks- and Tazo-branded K-Cup® portion packs. Operating income grew $33 million, or 35%, to $127 million. Operating margin increased 660 basis points to 34.4% for the second quarter of fiscal 2014, primarily driven by lower coffee costs and sales leverage. As we continue to expand customer occasions outside of our retail stores, including growing our presence in the premium single serve category, we expect this segment to become a more significant contributor to future growth.

Fiscal 2014 — Financial Outlook for the Year

For fiscal year 2014, we expect revenue growth will be driven by mid-single digit comparable store sales growth, new store openings, and continued growth in the Channel Development business. Approximately one-half of new store openings will be in China / Asia Pacific, with the remaining half coming primarily from the Americas.

We expect full-year consolidated operating margin improvement of 175 to 200 basis points over fiscal 2013 and strong EPS growth when excluding the Kraft litigation charge and gains from the sales of our equity in our Mexico, Chile and Argentina joint ventures in fiscal 2013.

Comparable Store Sales

Starbucks comparable store sales for the second quarter and the first two quarters of fiscal 2014:

	Quarter Ended Mar 30, 2014			Two Quarters Ended Mar 30, 2014		
	Sales Growth	Change in Transactions	Change in Ticket	Sales Growth	Change in Transactions	Change in Ticket
Consolidated	6%	3%	3%	6%	3%	2%
Americas	6%	2%	3%	5%	3%	2%
EMEA	6%	5%	1%	5%	4%	1%
China/Asia Pacific	7%	7%	—%	7%	7%	1%

Our comparable store sales represent the growth in revenue from Starbucks® company-operated stores open 13 months or longer. Comparable store sales exclude the effect of fluctuations in foreign currency exchange rates.

Results of Operations (in millions)

Revenues

	Quarter Ended			Two Quarters Ended		
	Mar 30, 2014	Mar 31, 2013	% Change	Mar 30, 2014	Mar 31, 2013	% Change
Company-operated stores	$3,068.0	$2,807.7	9.3 %	$6,411.8	$5,797.3	10.6 %
Licensed stores	356.2	322.1	10.6	758.0	672.2	12.8
CPG, foodservice and other	449.6	419.8	7.1	943.6	873.2	8.1
Total net revenues	$3,873.8	$3,549.6	9.1 %	$8,113.4	$7,342.7	10.5 %

Total net revenues for the second quarter and the first two quarters of fiscal 2014 increased $324 million and $771 million, respectively, primarily due to increased revenues from company-operated stores (contributing $260 million and $614 million, respectively). An increase in comparable store sales was the primary driver of the increase in company-operated store revenues (approximately 6% for both periods, or $152 million for the second quarter and $312 million for the first two quarters). Also contributing to net revenue growth for both periods were incremental revenues from 551 net new Starbucks® company-operated store openings over the past 12 months (approximately $127 million for the second quarter and $253 million for the first two quarters).

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Licensed store revenue growth also contributed to the increase in total net revenues for the second quarter and the first two quarters of fiscal 2014 (approximately $34 million for the second quarter and $86 million for the first two quarters). The increase for both periods was primarily due to increased product sales to and royalty revenues from our licensees, as a result of improved comparable store sales and the opening of 1,054 net new licensed stores over the past 12 months.

CPG, foodservice and other revenues increased $30 million and $70 million for the second quarter and the first two quarters of fiscal 2014, respectively. These increases were primarily due to increased sales of premium single serve products (approximately $23 million and $48 million, respectively).

Operating Expenses

	Quarter Ended				Two Quarters Ended			
	Mar 30, 2014	Mar 31, 2013	Mar 30, 2014	Mar 31, 2013	Mar 30, 2014	Mar 31, 2013	Mar 30, 2014	Mar 31, 2013
			% of Total Net Revenues				% of Total Net Revenues	
Cost of sales including occupancy costs	$1,629.2	$1,530.4	42.1 %	43.1 %	$3,424.2	$3,151.1	42.2 %	42.9 %
Store operating expenses	1,134.5	1,038.4	29.3	29.3	2,309.6	2,127.9	28.5	29.0
Other operating expenses	110.9	105.8	2.9	3.0	225.8	231.9	2.8	3.2
Depreciation and amortization expenses	174.4	153.1	4.5	4.3	344.1	302.0	4.2	4.1
General and administrative expenses	240.6	230.3	6.2	6.5	483.2	462.2	6.0	6.3
Litigation charge/(credit)	—	—	—	—	(20.2)	—	(0.2)	—
Total operating expenses	3,289.6	3,058.0	84.9	86.2	6,766.7	6,275.1	83.4	85.5
Income from equity investees	59.9	52.5	1.5	1.5	111.0	107.0	1.4	1.5
Operating income	$644.1	$544.1	16.6 %	15.3 %	$1,457.7	$1,174.6	18.0 %	16.0 %
Store operating expenses as a % of related revenues			37.0 %	37.0 %			36.0 %	36.7 %

Cost of sales including occupancy costs as a percentage of total net revenues decreased 100 basis points and 70 basis points for the second quarter and first two quarters of fiscal 2014, respectively, primarily driven by lower commodity costs (approximately 100 basis points for the second quarter and 90 basis points for the first two quarters), mainly coffee.

Store operating expenses as a percentage of total net revenues were flat for the second quarter and decreased 50 basis points for the first two quarters of fiscal 2014. Store operating expenses as a percentage of company-operated store revenues were flat for the second quarter and decreased 70 basis points for the first two quarters of fiscal 2014. The decrease for the first two quarters of fiscal 2014 was primarily driven by higher litigation charges in the first quarter of the prior year period (approximately 40 basis points) and a decrease in marketing (approximately 20 basis points), largely due to lapping the prior year launch of the Verismo® system by Starbucks in company-operated stores.

Other operating expenses as a percentage of total net revenues decreased 10 basis points for the second quarter and 40 basis points for the first two quarters of fiscal 2014. Excluding the impact of company-operated store revenues, other operating expenses decreased 50 basis points for the second quarter and 170 basis points for the first two quarters of fiscal 2014, primarily due to decreased marketing (approximately 20 basis points for the second quarter and 60 basis points for the first two quarters). The decrease for the first two quarters of fiscal 2014 was primarily attributable to the timing of product launches in Channel Development. Sales leverage from licensed store revenue growth (approximately 20 basis points for the second quarter and 30 basis points for the first two quarters) also contributed to the decreases.

General and administrative expenses as a percentage of total net revenues decreased 30 basis points for both the second quarter and the first two quarters of fiscal 2014. The decrease for the second quarter was primarily due to increased sales leverage. The decrease for the first two quarters was primarily due to lapping our leadership conference held in the first quarter of the prior year period.

The $20.2 million litigation credit (contributing approximately 20 basis points for the first two quarters of fiscal 2014) reflects a reduction to our estimated prejudgment interest payable associated with the Kraft arbitration in the first quarter of fiscal 2014, as a result of paying our obligation earlier than anticipated. The $2.8 billion litigation charge was accrued in the fourth quarter of fiscal 2013 and fully extinguished in the first quarter of fiscal 2014.

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The combination of these changes resulted in an overall increase in operating margin of 130 basis points for the second quarter and 200 basis points for the first two quarters of fiscal 2014.

Other Income and Expenses

	Quarter Ended				Two Quarters Ended			
	Mar 30, 2014	Mar 31, 2013	Mar 30, 2014	Mar 31, 2013	Mar 30, 2014	Mar 31, 2013	Mar 30, 2014	Mar 31, 2013
			% of Total Net Revenues				% of Total Net Revenues	
Operating income	$644.1	$544.1	16.6 %	15.3 %	$1,457.7	$1,174.6	18.0 %	16.0 %
Interest income and other, net	17.8	50.8	0.5	1.4	37.6	48.0	0.5	0.7
Interest expense	(16.7)	(6.1)	(0.4)	(0.2)	(31.3)	(12.7)	(0.4)	(0.2)
Earnings before income taxes	645.2	588.8	16.7	16.6	1,464.0	1,209.9	18.0	16.5
Income taxes	218.3	198.1	5.6	5.6	496.4	386.8	6.1	5.3
Net earnings including noncontrolling interests	426.9	390.7	11.0	11.0	967.6	823.1	11.9	11.2
Net earnings attributable to noncontrolling interests	(0.1)	0.3	—	—	—	0.6	—	—
Net earnings attributable to Starbucks	$427.0	$390.4	11.0 %	11.0 %	$967.6	$822.5	11.9 %	11.2 %
Effective tax rate including noncontrolling interests			33.8 %	33.6 %			33.9 %	32.0 %

For the second quarter and first two quarters of fiscal 2014, net interest income and other decreased $33 million and $10 million, respectively. These decreases were primarily due to lapping the gain on the sale of our equity in the joint venture that operates Starbucks® stores in Mexico in the prior year quarter (approximately $35 million). Also contributing to the decreases were unrealized losses on our trading securities portfolio (approximately $14 million for the second quarter and $10 million for the first two quarters), partially offset by favorable mark-to-market adjustments from derivatives used to manage our risk of commodity price fluctuations (approximately $8 million for the second quarter and $17 million for the first two quarters).

Interest expense increased $11 million for the second quarter and $19 million for the first two quarters of fiscal 2014, respectively, due to interest on the long-term debt we issued in the first quarter of fiscal 2014 and the fourth quarter of fiscal 2013.

The effective tax rate for the quarter ended March 30, 2014 was 33.8% compared to 33.6% for the same quarter in fiscal 2013. The slight increase in the rate was driven by the release of a capital loss valuation allowance in the prior year period. The effective tax rate for the two quarters ended March 30, 2014 was 33.9% compared to 32.0% for the same period in fiscal 2013. The increase in the rate for the first two quarters of fiscal 2014 was primarily due to lapping the recognition of a net tax benefit in the first quarter of fiscal 2013 primarily from state income tax expense adjustments for returns filed in prior years.

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Segment Information

Results of operations by segment (in millions):

Americas

	Quarter Ended				Two Quarters Ended			
	Mar 30, 2014	Mar 31, 2013	Mar 30, 2014	Mar 31, 2013	Mar 30, 2014	Mar 31, 2013	Mar 30, 2014	Mar 31, 2013
			% of Americas Net Revenues				% of Americas Net Revenues	
Total net revenues	$2,808.8	$2,604.1			$5,881.7	$5,444.7		
Cost of sales including occupancy costs	1,059.6	1,000.0	37.7 %	38.4 %	2,223.8	2,092.5	37.8 %	38.4 %
Store operating expenses	963.9	891.9	34.3	34.2	1,963.5	1,851.7	33.4	34.0
Other operating expenses	23.7	21.2	0.8	0.8	49.0	51.2	0.8	0.9
Depreciation and amortization expenses	114.8	105.6	4.1	4.1	227.1	211.0	3.9	3.9
General and administrative expenses	41.2	38.1	1.5	1.5	80.7	100.9	1.4	1.9
Total operating expenses	2,203.2	2,056.8	78.4	79.0	4,544.1	4,307.3	77.3	79.1
Income from equity investees	—	2.4	—	0.1	—	2.4	—	—
Operating income	$605.6	$549.7	21.6 %	21.1 %	$1,337.6	$1,139.8	22.7 %	20.9 %
Store operating expenses as a % of related revenues			37.6 %	37.5 %			36.7 %	37.3 %

Revenues

Americas total net revenues for the second quarter and the first two quarters of fiscal 2014 increased 8% for both periods or $205 million and $437 million, respectively. These increases were primarily due to higher revenues from company-operated stores (contributing $185 million and $386 million, respectively) and licensed stores (contributing $21 million and $56 million, respectively).

The increase in company-operated store revenues for both periods was driven by an increase in comparable store sales (approximately 6%, or $129 million, for the second quarter and approximately 5%, or $265 million, for the first two quarters). Also contributing were incremental revenues from 311 net new Starbucks® company-operated store openings over the past 12 months (approximately $88 million and $178 million, respectively). Partially offsetting these increases was unfavorable foreign currency exchange (approximately $21 million and $37 million, respectively), primarily driven by the strengthening of the US dollar against the Canadian dollar.

The increases in licensed store revenues were primarily due to increased product sales to and higher royalty revenues from our licensees, as a result of improved comparable store sales and the opening of 456 net new licensed stores over the past 12 months.

Operating Expenses

Cost of sales including occupancy costs as a percentage of total net revenues decreased 70 basis points and 60 basis points for the second quarter and the first two quarters of fiscal 2014, respectively. These decreases were primarily driven by lower commodity costs (approximately 60 basis points for the second quarter and 50 basis points for the first two quarters). Sales leverage on occupancy costs also contributed.

Store operating expenses as a percentage of total net revenues and as a percentage of company-operated store revenues, increased 10 basis points for the second quarter and decreased 60 basis points for the first two quarters of fiscal 2014. The slight increase for the second quarter was primarily driven by timing of marketing (20 basis points). The decrease for the first two quarters of fiscal 2014 was primarily driven by higher litigation charges in the first quarter of the prior year period (approximately 40 basis points) and a decrease in marketing (approximately 20 basis points), largely due to lapping the prior year launch of the Verismo® system by Starbucks in company-operated stores.

General and administrative expenses as a percentage of total net revenues were flat for the second quarter and decreased 50 basis points for the first two quarters of fiscal 2014, primarily due to lapping our leadership conference held in the first quarter of the prior year period (approximately 40 basis points).

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The combination of these changes resulted in an overall increase in operating margin of 50 basis points for the second quarter and 180 basis points for the first two quarters of fiscal 2014.

EMEA

	Quarter Ended				Two Quarters Ended			
	Mar 30, 2014	Mar 31, 2013	Mar 30, 2014	Mar 31, 2013	Mar 30, 2014	Mar 31, 2013	Mar 30, 2014	Mar 31, 2013
			% of EMEA Net Revenues				% of EMEA Net Revenues	
Total net revenues	$309.9	$273.2			$649.5	$579.3		
Cost of sales including occupancy costs	158.3	140.8	51.1 %	51.5 %	326.5	293.3	50.3 %	50.6 %
Store operating expenses	92.4	83.2	29.8	30.5	188.8	173.5	29.1	29.9
Other operating expenses	11.8	10.7	3.8	3.9	23.4	19.1	3.6	3.3
Depreciation and amortization expenses	14.8	13.7	4.8	5.0	29.4	27.9	4.5	4.8
General and administrative expenses	16.0	19.6	5.2	7.2	32.1	38.0	4.9	6.6
Total operating expenses	293.3	268.0	94.6	98.1	600.2	551.8	92.4	95.3
Income from equity investees	1.1	—	0.4	—	1.9	—	0.3	—
Operating income	$17.7	$5.2	5.7 %	1.9 %	$51.2	$27.5	7.9 %	4.7 %
Store operating expenses as a % of related revenues			37.6 %	38.0 %			36.7 %	36.8 %

Revenues

EMEA total net revenues increased $37 million, or 13%, for the second quarter of fiscal 2014 and increased $70 million, or 12%, for the first two quarters of fiscal 2014. These increases were primarily due to higher revenues from company-operated stores (contributing $27 million and $43 million, respectively). These increases were driven by an increase in comparable store sales (approximately 6%, or $12 million, for the second quarter and approximately 5%, or $24 million, for the first two quarters) and favorable foreign currency exchange (approximately $12 million and $19 million, respectively), primarily driven by the weakening of the US dollar against the British pound.

Licensed store revenues grew (approximately $8 million, or 18%, for the second quarter and $25 million, or 28%, for the first two quarters), due to increased equipment and product sales to and higher royalty revenues from our licensees, primarily from the opening of 168 net new licensed stores over the past 12 months and improved comparable store sales.

Operating Expenses

Cost of sales including occupancy costs as a percentage of total net revenues decreased 40 basis points for the second quarter and 30 basis points for the first two quarters of fiscal 2014, primarily driven by sales leverage and continued cost management (approximately 110 basis points for the second quarter and 100 basis points for the first two quarters). Also contributing to the decreases were lapping higher inventory reserves in the prior year (approximately 80 basis points for the second quarter and 40 basis points for the first two quarters) and lower coffee costs (approximately 60 basis points for both periods), partially offset by lapping a reduction to the estimated asset retirement obligations of our store leases in the region in the second quarter of fiscal 2013 (approximately 190 basis points for the second quarter and 80 basis points for the first two quarters).

Store operating expenses as a percentage of total net revenues decreased 70 basis points and 80 basis points for the second quarter and the first two quarters of fiscal 2014, respectively. These decreases were driven by sales leverage. As a percentage of company-operated store revenues, store operating expenses decreased 40 basis points for the second quarter and 10 basis point for the first two quarters of fiscal 2014.

Other operating expenses as a percentage of total net revenues decreased 10 basis points for the second quarter and increased 30 basis points for the first two quarters of fiscal 2014. Excluding the impact of company-operated store

revenues, other operating expenses decreased 140 basis points for the second quarter and 50 basis points for the first two quarters, primarily driven by sales leverage and continued cost management (approximately 100 basis points for both periods).

General and administrative expenses as a percentage of total net revenues decreased 200 basis points and 170 basis points for the second quarter and the first two quarters of fiscal 2014, respectively. These decreases were primarily due to sales leverage

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and reduced support costs, largely driven by the shift to more licensed stores (approximately 180 basis points for the second quarter and 170 basis points for the first two quarters of fiscal 2014).
The combination of these changes resulted in an overall increase in operating margin of 380 basis points for the second quarter and 320 basis points for the first two quarters of fiscal 2014.
China / Asia Pacific

	Quarter Ended				Two Quarters Ended			
	Mar 30, 2014	Mar 31, 2013	Mar 30, 2014	Mar 31, 2013	Mar 30, 2014	Mar 31, 2013	Mar 30, 2014	Mar 31, 2013
			% of CAP Net Revenues				% of CAP Net Revenues	
Total net revenues	$265.3	$213.6			$532.2	$427.7		
Cost of sales including occupancy costs	127.4	104.9	48.0 %	49.1 %	260.2	211.4	48.9 %	49.4 %
Store operating expenses	52.4	40.3	19.8	18.9	103.7	79.7	19.5	18.6
Other operating expenses	11.1	11.5	4.2	5.4	21.7	21.7	4.1	5.1
Depreciation and amortization expenses	11.8	8.5	4.4	4.0	22.0	15.9	4.1	3.7
General and administrative expenses	13.0	10.9	4.9	5.1	27.1	23.5	5.1	5.5
Total operating expenses	215.7	176.1	81.3	82.4	434.7	352.2	81.7	82.3
Income from equity investees	37.4	30.8	14.1	14.4	70.5	64.9	13.2	15.2
Operating income	$87.0	$68.3	32.8 %	32.0 %	$168.0	$140.4	31.6 %	32.8 %
Store operating expenses as a % of related revenues			25.9 %	25.8 %			25.7 %	26.0 %

Revenues
China/Asia Pacific total net revenues for the second quarter and the first two quarters of fiscal 2014 increased $52 million, or 24%, and $105 million, or 24%, respectively, primarily due to increased revenues from company-operated stores (contributing $46 million for the second quarter and $97 million for the first two quarters). The increases in company-operated store revenues were primarily driven by the opening of 241 net new company-operated stores over the past 12 months (approximately $37 million for the second quarter and $75 million for the first two quarters) and an increase in comparable store sales (approximately 7% for both periods, or $11 million for the second quarter and $23 million for the first two quarters).
Operating Expenses
Cost of sales including occupancy costs as a percentage of total net revenues decreased 110 basis points for the second quarter of fiscal 2014 and 50 basis points for the first two quarters of fiscal 2014, primarily due to sales leverage.
Store operating expenses as a percentage of total net revenues increased 90 basis points for both the second quarter and the first two quarters of fiscal 2014. As a percentage of company-operated store revenues, store operating expenses increased 10 basis points for the second quarter, primarily driven by increased costs associated with company-operated store growth (approximately 50 basis points), partially offset by an insurance claim credit in the current quarter (approximately 40 basis points). As a percentage of company-operated store revenues, store operating expenses decreased 30 basis points for the first two quarters of fiscal 2014, primarily driven by the insurance claim credit in the second quarter of fiscal 2014 (approximately 20 basis points).
Other operating expenses as a percentage of total net revenues decreased 120 basis points for the second quarter of fiscal 2014 and 100 basis points for the first two quarters of fiscal 2014. Excluding the impact of company-operated store revenues, other operating expenses decreased 240 basis points for the second quarter and 110 basis points for the first two quarters. These decreases were primarily due to sales leverage.

Income from equity investees increased $7 million for the second quarter of fiscal 2014 and $6 million for the first two quarters of fiscal 2014, driven by higher income from our joint venture operations, mainly in South Korea and China, partially offset by unfavorable foreign currency fluctuations due to the weakening of the Yen against the US dollar. These fluctuations, paired with the accelerated growth in segment revenues resulting from the shift in the composition of the store portfolio to more company-operated stores, resulted in income from equity investees declining as a percentage of total net revenues.

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The changes in the above items resulted in an overall increase in operating margin of 80 basis points for the second quarter of fiscal 2014 and a decrease of 120 basis points for the first two quarters of 2014.

Channel Development

	Quarter Ended				Two Quarters Ended			
	Mar 30, 2014	Mar 31, 2013	Mar 30, 2014	Mar 31, 2013	Mar 30, 2014	Mar 31, 2013	Mar 30, 2014	Mar 31, 2013
			% of Channel Development Net Revenues				% of Channel Development Net Revenues	
Total net revenues	$370.4	$338.1			$771.5	$712.5		
Cost of sales	213.6	212.6	57.7 %	62.9 %	459.2	447.8	59.5 %	62.8 %
Other operating expenses	46.6	43.9	12.6	13.0	94.6	101.5	12.3	14.2
Depreciation and amortization expenses	0.4	0.3	0.1	0.1	0.8	0.6	0.1	0.1
General and administrative expenses	3.9	6.5	1.1	1.9	9.3	11.3	1.2	1.6
Total operating expenses	264.5	263.3	71.4	77.9	563.9	561.2	73.1	78.8
Income from equity investees	21.4	19.3	5.8	5.7	38.6	39.7	5.0	5.6
Operating income	$127.3	$94.1	34.4 %	27.8 %	$246.2	$191.0	31.9 %	26.8 %

Revenues

Total Channel Development net revenues for the second quarter and the first two quarters of fiscal 2014 increased $32 million, or 10%, and $59 million, or 8%, respectively, primarily driven by increased sales of premium single serve products (approximately $23 million for the second quarter and $48 million for the first two quarters). Also contributing was an increase in foodservice revenues (approximately $5 million for the second quarter and $13 million for the first two quarters) driven by increased sales volumes compared to the prior year period. The increased sales for the first two quarters of fiscal 2014 were partially offset by the impact of the packaged coffee list price reductions (approximately $14 million) effective beginning in the third quarter of fiscal 2013.

Operating Expenses

Cost of sales as a percentage of total net revenues decreased 520 basis points for the second quarter and 330 basis points for the first two quarters of fiscal 2014. The decrease was primarily driven by lower coffee costs (approximately 510 basis points for the second quarter and 420 basis points for the first two quarters). The decrease for the first two quarters was partially offset by the impact of the list price reductions on total net revenues (approximately 100 basis points).

Other operating expenses as a percentage of total net revenues decreased 40 basis points for the second quarter and 190 basis points for the first two quarters of fiscal 2014. The decrease for the second quarter was primarily due to sales leverage. The decrease for the first two quarters was primarily due to decreased marketing (approximately 100 basis points), largely due to the timing of product launches.

Income from equity investees increased $2 million for the second quarter of fiscal 2014 and decreased $1 million for the first two quarters of fiscal 2014. The increase for the second quarter was a result of higher income from our North American Coffee Partnership joint venture, primarily due to strong sales of bottled Frappuccino® and iced coffee drinks. The decrease for the first two quarters was a result of lower income from our North American Coffee Partnership joint venture, driven by increased investment in support of new product innovation platforms in the first quarter of fiscal 2014. The growth in segment revenues also contributed to our joint venture income declining as a percentage of total net revenues for the first two quarters of fiscal 2014.

The combination of these changes resulted in an overall increase in operating margin of 660 basis points for the second quarter and 510 basis points for the first two quarters of fiscal 2014.

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All Other Segments

	Quarter Ended			Two Quarters Ended		
	Mar 30, 2014	Mar 31, 2013	% Change	Mar 30, 2014	Mar 31, 2013	% Change
Total net revenues	$119.4	$120.6	(1.0)%	$278.5	$178.5	56.0%
Cost of sales	68.8	69.7	(1.3)	151.3	106.0	42.7
Store operating expenses	25.8	23.0	12.2	53.6	23.0	133.0
Other operating expenses	18.0	18.5	(2.7)	37.6	38.4	(2.1)
Depreciation and amortization expenses	3.7	3.4	8.8	7.3	4.3	69.8
General and administrative expenses	10.9	10.1	7.9	22.6	15.0	50.7
Total operating expenses	127.2	124.7	2.0	272.4	186.7	45.9
Operating income/(loss)	$(7.8)	$(4.1)	90.2%	$6.1	$(8.2)	nm

All Other Segments includes Teavana, Seattle's Best Coffee, Evolution Fresh, and Digital Ventures.

Total net revenues for All Other Segments decreased $1 million for the second quarter of fiscal 2014 and increased $100 million for the first two quarters of fiscal 2014. The decrease for the second quarter resulted from lower Seattle's Best Coffee revenues (approximately $10 million) mostly offset by growth in emerging businesses (approximately $6 million), including Teavana and Evolution Fresh. The increase for the first two quarters was primarily driven by having an additional quarter of Teavana revenues in fiscal 2014 as Teavana was acquired at the beginning of the second quarter of fiscal 2013 (approximately $92 million).

Total operating expenses increased $3 million for the second quarter and $86 million for the first two quarters of fiscal 2014. The increase for the second quarter was driven by investments to support our emerging businesses. The increase for the first two quarters was primarily due to having an additional quarter of Teavana expenses in fiscal 2014 as Teavana was acquired at the beginning of the second quarter of fiscal 2013.

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Quarterly Store Data

Our store data for the periods presented is as follows:

	Net stores opened/(closed) during the period					
	Quarter Ended		Two Quarters Ended		Stores open as of	
	Mar 30, 2014	Mar 31, 2013	Mar 30, 2014	Mar 31, 2013	Mar 30, 2014	Mar 31, 2013
Americas						
Company-operated stores	59	24	86	50	8,164	7,852
Licensed stores	69	71	184	132	5,599	5,143
Total Americas	128	95	270	182	13,763	12,995
EMEA[1]						
Company-operated stores	1	(4)	4	(24)	842	843
Licensed stores	31	26	92	53	1,223	1,055
Total EMEA	32	22	96	29	2,065	1,898
China / Asia Pacific						
Company-operated stores	53	66	114	113	1,020	779
Licensed stores	121	81	269	159	3,245	2,787
Total China / Asia Pacific	174	147	383	272	4,265	3,566
All Other Segments [2]						
Company-operated stores	4	306	11	309	368	323
Licensed stores	(3)	20	(8)	10	58	86
Total All Other Segments	1	326	3	319	426	409
Total Company	335	590	752	802	20,519	18,868

[1] EMEA store data has been adjusted for the transfer of certain company-operated stores to licensed stores in the second quarter of fiscal 2014.

[2] Includes 337 Teavana stores added in the second quarter of fiscal 2013.

Financial Condition, Liquidity and Capital Resources

Investment Overview

Starbucks cash and short-term investments totaled $1.5 billion and $3.2 billion as of March 30, 2014 and September 29, 2013, respectively. As discussed below, in the first quarter of fiscal 2014 we paid $2.8 billion for the Kraft arbitration matter that was accrued in the fourth quarter of fiscal 2013. We actively manage our cash and short-term investments in order to internally fund operating needs, make scheduled interest and principal payments on our borrowings, and return cash to shareholders through common stock cash dividend payments and share repurchases. Our short-term and long-term investments consist of highly liquid available-for-sale securities, including agency obligations, corporate bonds, government treasury securities (foreign and domestic), state and local government obligations, mortgage and asset-backed securities, commercial paper, mutual funds, and certificates of deposit. As of March 30, 2014, approximately $1.1 billion of cash and investments was held in foreign subsidiaries.

Borrowing Capacity

In December 2013, we issued $400 million of 3-year 0.875% Senior Notes ("the 2014 3-year notes") due December 2016, and $350 million of 5-year 2.000% Senior Notes ("the 2014 5-year notes") due December 2018, in an underwritten registered public offering, to fund a portion of the payment required by the arbitration award in the Kraft litigation matter. The remaining net proceeds will be used for general corporate purposes, which may include business expansion, payment of cash dividends on our common stock, the repurchase of common stock under our ongoing share repurchase program, or financing of possible acquisitions. Interest on the notes is payable semi-annually on June 5 and December 5 of each year, commencing on June 5, 2014. See Note 6, Debt, to the condensed consolidated financial statements included in Item 1 of Part I of this 10-Q for details of the components of our long-term debt.

The indentures under which all of our Senior Notes were issued require us to maintain compliance with certain covenants, including limits on future liens and sale and leaseback transactions on certain material properties. As of March 30, 2014, we were in compliance with each of these covenants.

Our $750 million unsecured, revolving credit facility with various banks, of which $150 million may be used for issuances of letters of credit, is available for working capital, capital expenditures and other corporate purposes, including acquisitions and share repurchases, and is currently set to mature on February 5, 2018. Starbucks has the option, subject to negotiation and agreement with the related banks, to increase the maximum commitment amount by an additional $750 million. Borrowings under the credit facility will bear interest at a variable rate based on LIBOR, and, for US dollar-denominated loans under certain circumstances, a Base Rate (as defined in the credit facility), in each case plus an applicable margin. The applicable margin is based on the better of (i) the Company's long-term credit ratings assigned by Moody's and Standard & Poor's rating agencies, and (ii) the Company's fixed charge coverage ratio, pursuant to a pricing grid set forth in the credit facility. The current applicable margin is 0.795% for Eurocurrency Rate Loans and 0.00% for Base Rate Loans. The credit facility contains provisions requiring us to maintain compliance with certain covenants, including a minimum fixed charge coverage ratio, which measures our ability to cover financing expenses. As of March 30, 2014, we were in compliance with each of these covenants. No amounts were outstanding under our credit facility as of March 30, 2014.

Under our commercial paper program, as approved by our Board of Directors, we may issue unsecured commercial paper notes up to a maximum aggregate amount outstanding at any time of $1 billion, with individual maturities that may vary but not exceed 397 days from the date of issue. Amounts outstanding under the commercial paper program are to be backstopped by available commitments under our credit facility. Currently, we may issue up to $727 million under our commercial paper program (the $750 million committed credit facility amount, less $23 million in outstanding letters of credit). The proceeds from borrowings under our commercial paper program may be used for working capital needs, capital expenditures and other corporate purposes, including acquisitions and share repurchases. In the first quarter of fiscal 2014, we issued and subsequently repaid commercial paper borrowings of $225 million to fund a portion of the $2.8 billion payment for the Kraft arbitration matter. We had no borrowings under our commercial paper program during the second quarter of fiscal 2014.

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Use of Cash

In the first quarter of fiscal 2014, Starbucks paid all amounts due to Kraft under the arbitration, including prejudgment interest and attorneys' fees, and fully extinguished the litigation charge liability. Of the $2,784.1 million litigation charge accrued in the fourth quarter of fiscal 2013, $2,763.9 million was paid and the remainder was released as a litigation credit to reflect a reduction to our estimated prejudgment interest payable as a result of paying our obligation earlier than anticipated.

We expect to use additional available cash and short-term investments, including additional potential future borrowings under the credit facility and commercial paper program, to invest in our core businesses, including new product innovations and related marketing support, as well as other new business opportunities related to our core businesses. We believe that future cash flows generated from operations and existing cash and short-term investments both domestically and internationally will be sufficient to finance capital requirements for our core businesses in those respective markets as well as shareholder distributions for the foreseeable future.

We consider the majority of undistributed earnings of our foreign subsidiaries and equity investees as of March 30, 2014 to be indefinitely reinvested and, accordingly, no US income and foreign withholding taxes have been provided on such earnings. We have not, nor do we anticipate the need to, repatriate funds to the US to satisfy domestic liquidity needs; however, in the event that we need to repatriate all or a portion of our foreign cash to the US we would be subject to additional US income taxes, which could be material. We do not believe it is practical to calculate the potential tax impact of repatriation, as there is a significant amount of uncertainty around the calculation, including the availability and amount of foreign tax credits at the time of repatriation, tax rates in effect, and other indirect tax consequences associated with repatriation.

We may use our available cash resources to make proportionate capital contributions to our equity method and cost method investees. We may also seek strategic acquisitions to leverage existing capabilities and further build our business in support of our growth agenda. Acquisitions may include increasing our ownership interests in our equity method and cost method investees. Any decisions to increase such ownership interests will be driven by valuation and fit with our ownership strategy. Significant new joint ventures, acquisitions and/or other new business opportunities may require additional outside funding.

Other than normal operating expenses, cash requirements for the remainder of fiscal 2014 are expected to consist primarily of capital expenditures for remodeling and refurbishment of, and equipment upgrades for, existing company-operated stores; new company-operated stores; systems and technology investments in the stores and in the support infrastructure; and additional investments in manufacturing capacity. Total capital expenditures for fiscal 2014 are expected to be approximately $1.2 billion.

During the second quarter of fiscal 2014, our Board of Directors declared a quarterly cash dividend to shareholders of $0.26 per share to be paid on May 23, 2014 to shareholders of record as of the close of business on May 8, 2014. We repurchased 4.1 million shares of common stock ($301.2 million) during the first two quarters of fiscal 2014 under share repurchase authorizations. The number of remaining shares authorized for repurchase as of March 30, 2014 totaled 22.3 million.

Cash Flows

Cash used by operating activities was $983.5 million for the first two quarters of fiscal 2014, compared to cash provided by operating activities of $1.4 billion for the same period in fiscal 2013. The decrease was driven by the first quarter payment of $2.8 billion for the Kraft arbitration matter discussed above. This was partially offset by cash provided by operating activities of $1.8 billion resulting from increased earnings and improvements in working capital accounts.

Cash used by investing activities for the first two quarters of fiscal 2014 totaled $549.0 million, compared to $613.0 million for the same period in fiscal 2013. The change was primarily due to the use of cash to acquire Teavana in the second quarter of fiscal 2013, partially offset by increased investment in long-term securities during the first two quarters of fiscal 2014.

Cash provided by financing activities for the first two quarters of fiscal 2014 totaled $157.4 million, compared to cash used by financing activities of $718.5 million for the same period in fiscal 2013. The increase was primarily due to the proceeds from the issuance of long-term debt in the first quarter of fiscal 2014 and decreased share repurchases

compared to the first two quarters of fiscal 2013.

Contractual Obligations

In Management's Discussion and Analysis of Financial Condition and Results of Operations included in the 10-K, we disclosed that we had $10.0 billion in total contractual obligations as of September 29, 2013. Other than the items discussed below, there have been no material changes to this total obligation during the period covered by this 10-Q outside of the ordinary course of our business.

In the first quarter of fiscal 2014, we issued $750 million of debt, as described in Note 6 to the condensed consolidated financial statements included in Item 1 of Part I of this 10-Q. In addition, the $2.8 billion that was accrued for the Kraft arbitration matter as of September 29, 2013 was removed from total contractual obligations, as this obligation was fully extinguished in the first quarter of fiscal 2014.

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Off-Balance Sheet Arrangements

There has been no material change in our off-balance sheet arrangements discussed in Management's Discussion and Analysis of Financial Condition and Results of Operations included in the 10-K.

Commodity Prices, Availability and General Risk Conditions

Commodity price risk represents our primary market risk, generated by our purchases of green coffee and dairy products, among other items. We purchase, roast and sell high quality whole bean arabica coffee and related products and risk arises from the price volatility of green coffee. In addition to coffee, we also purchase significant amounts of dairy products to support the needs of our company-operated stores. The price and availability of these commodities directly impact our results of operations and we expect commodity prices, particularly coffee, to impact future results of operations. For additional details see Product Supply in Item 1 of the 10-K, as well as Risk Factors in Item 1A of the 10-K.

Seasonality and Quarterly Results

Our business is subject to seasonal fluctuations, including fluctuations resulting from the holiday season in December. Notwithstanding our $2.8 billion cash payment in the first quarter of 2014 related to the Kraft arbitration matter, our cash flows from operations are considerably higher in the first fiscal quarter than the remainder of the year. This is largely driven by cash received as Starbucks Cards are purchased and loaded during the holiday season. Since revenues from the Starbucks Card are recognized upon redemption and not when purchased, seasonal fluctuations on the consolidated statements of earnings are much less pronounced. Quarterly results are affected by the timing of the opening of new stores and the closing of existing stores. For these reasons, results for any quarter are not necessarily indicative of the results that may be achieved for the full fiscal year.

RECENT ACCOUNTING PRONOUNCEMENTS

See Note 1 to the condensed consolidated financial statements included in Item 1 of Part I of this 10-Q.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

There has been no material change in the commodity price risk, foreign currency exchange risk, equity security price risk, or interest rate risk discussed in Item 7A of the 10-K.

Item 4. Controls and Procedures

We maintain disclosure controls and procedures that are designed to ensure that material information required to be disclosed in our periodic reports filed or submitted under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms. Our disclosure controls and procedures are also designed to ensure that information required to be disclosed in the reports we file or submit under the Exchange Act is accumulated and communicated to our management, including our principal executive officer and principal financial officer as appropriate, to allow timely decisions regarding required disclosure.

During the second quarter of fiscal 2014, we carried out an evaluation, under the supervision and with the participation of our management, including our chief executive officer and our chief financial officer, of the effectiveness of the design and operation of the disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act. Based upon that evaluation, our chief executive officer and chief financial officer concluded that our disclosure controls and procedures were effective, as of the end of the period covered by this report (March 30, 2014).

There were no changes in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) of the Exchange Act) during our most recently completed fiscal quarter that materially affected or are reasonably likely to materially affect internal control over financial reporting.

The certifications required by Section 302 of the Sarbanes-Oxley Act of 2002 are filed as exhibits 31.1 and 31.2 to this 10-Q.

PART II — OTHER INFORMATION

Item 1. Legal Proceedings

See Note 10 to the condensed consolidated financial statements included in Item 1 of Part I of this 10-Q for information regarding certain legal proceedings in which we are involved.

Item 1A. Risk Factors

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There have been no material changes to the risk factors previously disclosed in the 10-K.

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

Information regarding repurchases of our common stock during the quarter ended March 30, 2014:

	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs [(2)]
Period[(1)]				
December 30, 2013 — January 26, 2014	1,025,288	$75.97	1,025,288	24,729,132
January 27, 2014 — February 23, 2014	1,276,100	72.50	1,276,100	23,453,032
February 24, 2014 — March 30, 2014	1,161,688	72.33	1,161,688	22,291,344
Total	3,463,076	$73.47	3,463,076	

(1) Monthly information is presented by reference to our fiscal months during the second quarter of fiscal 2014.

(2) The share repurchase program is conducted under authorizations made from time to time by our Board of Directors. On November 3, 2011, we publicly announced the authorization of up to an additional 20 million shares, and on November 15, 2012, we publicly announced the authorization of up to an additional 25 million shares. These authorizations have no expiration date.

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Item 6. Exhibits

Exhibit No.	Exhibit Description	Incorporated by Reference				Filed Herewith
		Form	File No.	Date of Filing	Exhibit Number	
3.1	Restated Articles of Incorporation of Starbucks Corporation	10-Q	0-20322	5/12/2006	3.1	
3.2	Amended and Restated Bylaws of Starbucks Corporation (As amended and restated through November 13, 2012)	10-K	0-20322	11/16/2012	3.2	
10.1	Letter Agreement dated January 29, 2014 between Starbucks Corporation and Troy Alstead	8-K	0-20322	1/29/2014	10.1	
10.2	Letter Agreement dated January 29, 2014 between Starbucks Corporation and Scott Maw	8-K	0-20322	1/29/2014	10.2	
10.3	Exclusive Aircraft Sublease (S/N 6003) dated as of September 27, 2013 by and between Cloverdale Services, LLC and Starbucks Corporation	—	—	—	—	X
31.1	Certification of Principal Executive Officer Pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, As Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	—	—	—	—	X
31.2	Certification of Principal Financial Officer Pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, As Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	—	—	—	—	X
32*	Certifications of Principal Executive Officer and Principal Financial Officer Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	—	—	—	—	—
101	The following financial statements from the Company’s 10-Q for the fiscal quarter ended March 30, 2014, formatted in XBRL: (i) Condensed Consolidated Statements of Earnings, (ii) Condensed Consolidated Statements of Comprehensive Income, (iii) Condensed Consolidated Balance Sheets, (iv) Condensed Consolidated Statements of Cash Flows and (v) Notes to Condensed Consolidated Financial Statements	—	—	—	—	X

* Furnished herewith.

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SIGNATURES

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.

April 29, 2014

STARBUCKS CORPORATION

By: /s/ Scott Maw
Scott Maw
executive vice president and chief financial officer
Signing on behalf of the registrant and as
principal financial officer

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)

$
—

$
11

State
142

140

94

Total income tax expense
$
46

$
140

$
105

The tax provisions for each of the years ended December 31, 2018, 2017 and 2016 are principally the result of minimum state taxes.

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PACIRA PHARMACEUTICALS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

A reconciliation of income taxes at the U.S. federal statutory rate to the provision for income taxes is as follows:

	Year Ended December 31,		
	2018	2017	2016
U.S. federal statutory rate	21.00 %	35.00 %	35.00 %
State taxes	(24.84)%	2.26 %	2.20 %
Foreign taxes	(92.04)%	(1.28)%	(0.81)%
Change in valuation allowance	369.27 %	4.58 %	(43.96)%
Stock-based compensation	(874.29)%	(1.21)%	(0.54)%
Tax credits	700.35 %	4.96 %	8.77 %
Interest expense	218.47 %	2.90 %	5.75 %
Effect of rate changes	13.44 %	(130.88)%	(4.65)%
Convertible senior notes refinancing	— %	6.55 %	— %
Effect of the adoption of ASU 2016-09	— %	68.89 %	— %
Nondeductible expenses	(132.96)%	— %	— %
Reserves	(202.98)%	— %	— %
Other	(6.15)%	7.90 %	(2.04)%
Effective tax rate	(10.73)%	(0.33)%	(0.28)%

The Company’s effective tax rates of (10.73)%, (0.33)% and (0.28)% for the years ended December 31, 2018, 2017 and 2016, respectively, differed from the expected U.S. statutory tax rate of 21.0% (previously 35.0%). This difference was primarily driven by pretax losses for which the Company concluded that a majority of its tax benefits are not more-likely-than-not to be realized, resulting in the recording of a full valuation allowance.

Deferred taxes reflect the tax effects of the differences between the amounts recorded as assets and liabilities for financial reporting purposes and the comparable amounts recorded for income tax purposes. Significant components of the Company’s deferred tax assets and liabilities at December 31, 2018 and 2017 are as follows (in thousands):

	December 31,	
	2018	2017
Deferred tax assets:		
Net operating loss carry-forwards	$79,446	$95,067
Federal and state credits	17,730	15,048
Depreciation and amortization	2,851	2,593
Accruals and reserves	11,009	2,743
Deferred revenue	—	1,841
Stock based compensation	18,302	16,925
Inventory	848	552
Other	127	139
Total deferred tax assets	130,313	134,908
Deferred tax liabilities:		
Discount on convertible senior notes	(11,655)	(14,678)
Deferred tax assets, net of deferred tax liabilities	118,658	120,230
Less: valuation allowance	(118,658)	(120,230)
Net deferred tax assets	$—	$—

As of December 31, 2018, the Company’s federal net operating losses, or NOLs, and federal tax credit carryforwards totaled $346.2 million and $12.7 million, respectively. The Company also had state NOLs and state tax credit carryforwards of $159.2 million and $6.3 million, respectively, which are subject to change on an annual basis due to variations in the

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PACIRA PHARMACEUTICALS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Company’s annual state apportionment factors. The Company had non-U.S. tax NOLs of $11.4 million at December 31, 2018. The existing federal NOLs will begin expiring in 2027 while the existing state NOLs begin expiring in 2024, if the Company has not used them prior to that time. The non-U.S. NOLs do not expire.

Since the Company had cumulative changes in ownership of more than 50% within a three-year period, under Internal Revenue Code sections 382 and 383, the Company’s ability to use certain net operating loss and credit carryforwards to offset taxable income or tax will be limited. Such ownership changes were triggered by the initial acquisition of the Company’s stock in 2007 as well as cumulative ownership changes arising as a result of the completion of the Company’s initial public offering and other financing transactions. As a result of these ownership changes, the Company estimates that approximately $191.1 million of federal net operating losses are subject to annual limitations. At December 31, 2018, $108.0 million of these federal net operating losses were available. The Company estimates that an additional $10.3 million will come available each year from 2019 through 2022, $3.5 million in 2023, $1.4 million each from 2024-2025 and that the remaining $35.8 million will expire unused. In addition, California and certain states have previously suspended or limited the use of NOL carryforwards for certain taxable years, and certain states are considering similar future measures. As a result, the Company may incur higher state income tax expense in the future.

In accordance with ASC Topic 740, the Company establishes a valuation allowance for deferred tax assets that, in its judgment, are not more-likely-than-not realizable. These judgments are based on projections of future income, including tax-planning strategies, by individual tax jurisdictions. In each reporting period, the Company assesses the likelihood that its deferred tax assets will be realized and determines if adjustments to its valuation allowance is appropriate. The Company had a net reduction in its valuation allowance of $1.6 million and $28.5 million in the years ended December 31, 2018 and 2017, respectively, and a net increase in its valuation allowance of $0.8 million for the year ended December 31, 2016. There is significant doubt regarding the Company’s ability to utilize its net deferred tax assets and, therefore, the Company has recorded a full valuation allowance reducing its net deferred tax assets to zero at both December 31, 2018 and 2017.

In December 2017, new legislation was signed into law reducing the corporate U.S. tax rate from 35% to 21% for tax years beginning after December 31, 2017, fully repealing the corporate alternative minimum tax and making the NOL carryforward period indefinite for NOLs generated after 2017. In accordance with ASC Topic 740, deferred tax assets and liabilities are required to be measured at the enacted tax rate expected to apply when temporary differences are to be realized or settled. As of December 31, 2017, the Company re-measured its deferred tax balances based upon the new 21% tax rate. This resulted in a reduction of $55.7 million in the Company’s deferred tax assets, which was offset by a change in its year-end valuation allowance.

In March 2017, the Company established a deferred tax liability with an offset to additional paid-in capital resulting from the conversion feature of the 2022 Notes. The initial difference between the book value of the convertible debt, issued with a beneficial conversion feature, and its tax basis was $70.9 million, a temporary difference. The net effect of the deferred tax liability recorded to additional paid-in capital was zero because the Company has a full valuation allowance against its net deferred tax assets.

In 2018, the Company recorded a reserve of $0.4 million related to unrecognized tax benefits, or UTBs, which relates to tax positions taken in 2018. The Company’s UTB liability at December 31, 2018 was $2.9 million. The change in the Company’s UTBs in 2018 is summarized as follows (in thousands):

	Unrecognized Tax Benefit
Balance at December 31, 2017	$ 2,473
Additions for current year positions	408
Balance at December 31, 2018	$ 2,881

The Company regularly assesses the likelihood of additional tax assessments by jurisdiction and, if necessary, adjusts its reserve for UTBs based on new information or developments. Due to the Company’s tax credit carryforwards, the

reserve was recorded as a reduction of the Company's deferred tax assets, and any potential deficiency would not result in a tax liability. Therefore, no interest or penalties were recognized in income tax expense for the years ended December 31, 2018 and 2017. Due to the Company's full valuation allowance against deferred tax assets, none of the UTBs, if recognized, would affect the effective income tax rate.

The Company estimates that it is not reasonably possible that within the next twelve months, any of the unrecognized tax benefits will significantly increase or decrease. The Company is currently subject to audit by the U.S. Internal Revenue Service,

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PACIRA PHARMACEUTICALS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

or IRS, for the years 2015 through 2018, and state tax jurisdictions for the years 2014 through 2018. However, the IRS or states may still examine and adjust an NOL arising from a closed year to the extent it is utilized in a year that remains subject to audit. The Company's previously filed income tax returns are not presently under audit by the IRS or state tax authorities.

NOTE 15—OTHER EMPLOYEE BENEFITS

The Company sponsors a 401(k) savings plan. Under this plan, employees may make contributions which are eligible for a discretionary percentage match as defined in the plan and determined by the Company's board of directors. The Company recognized $1.6 million, $1.3 million and $1.5 million of related compensation expense for the years ended December 31, 2018, 2017 and 2016, respectively.

NOTE 16—COMMERCIAL PARTNERS AND OTHER AGREEMENTS

DepoCyt(e) Discontinuation

In June 2017, the Company's board of directors approved a decision to discontinue production of DepoCyt® (U.S. and Canada) and DepoCyte® (E.U.) due to persistent technical issues specific to the DepoCyt(e) manufacturing process. As of June 30, 2017, the Company had ceased all production of DepoCyt(e).

In 2017, the Company recorded a non-recurring charge of $5.4 million related to the discontinuation of its DepoCyt(e) manufacturing activities, including $0.5 million for DepoCyt(e) related inventory, which is recorded in cost of goods sold, and $4.9 million was recorded in product discontinuation, including the remaining lease costs less an estimate of potential sublease income for the facility where DepoCyt(e) was manufactured, the write-off of property, plant and equipment, employee severance, asset retirement obligations and other estimated exit costs.

In 2018, the Company recorded a non-recurring charge of $1.6 million related to the discontinuation of its DepoCyt(e) manufacturing activities for lease costs, asset retirement obligations and other estimated exit costs. The charges incurred in 2018 represent additional lease and facility costs due to the fact that the Company does not expect to be able to sub-lease the property considering the short period of time remaining on the Company's existing lease.

Cash payments related to the lease on the DepoCyt(e) manufacturing facility are expected to continue through the end of the lease term in August 2020.

A summary of the Company's costs and reserves related to the DepoCyt(e) discontinuation are as follows (in thousands):

	Severance and Related Costs	Lease Costs	Write-Off of Property, Plant & Equipment and Inventory	Asset Retirement Obligations and Other Discontinuation Costs	Total
Balance at December 31, 2016	$ —	$—	$ —	$ —	$—
Charges incurred	303	2,018	2,470	656	5,447
Cash payments made	(303)	(744)	—	(420)	(1,467)
Disposal of property, plant & equipment and inventory	—	—	(2,470)	—	(2,470)
Balance sheet reclassifications	—	494	—	73	567
Balance at December 31, 2017	—	1,768	—	309	2,077

Charges incurred	—	1,513	—	51	1,564
Cash payments made	—	(1,311)	—	(91)	(1,402)
Balance sheet reclassifications	—	—	—	13	13
Balance at December 31, 2018	$ —	$1,970	$ —	$ 282	$2,252

Prior to the discontinuation, the Company received a fixed payment for the supply of DepoCyt(e) and double-digit royalties, net of supply price, on the sales of DepoCyt by Leadiant Bioscience, Ltd. in the U.S. and Canada, and on the sales of DepoCyte by Mundipharma International Corporation Limited, or Mundipharma, in the E.U. and other European countries. In

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PACIRA PHARMACEUTICALS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

addition, the Company also received a non-refundable upfront payment of $8.0 million in connection with a 15 year extension and concurrent expansion of the territories where Mundipharma can market and distribute DepoCyte. In April 2018, the Company received formal notice of the termination of the supply and distribution agreements (and all related agreements) from Mundipharma and its affiliates. The Company may be required to make additional payments or incur additional costs relating to the DepoCyt(e) discontinuation which could be material to the Company's results of operations and/or cash flows in a given period.

Commercial Partners

Thermo Fisher Scientific Pharma Services (Formerly Patheon UK Limited)

In April 2014, the Company and Thermo Fisher Scientific Pharma Services (formerly Patheon UK Limited), or Thermo Fisher, entered into a Strategic Co-Production Agreement, a Technical Transfer and Service Agreement and a Manufacturing and Supply Agreement to collaborate in the manufacture of EXPAREL. Under the terms of the Technical Transfer and Service Agreement, Thermo Fisher agreed to undertake certain technical transfer activities and construction services needed to prepare its Swindon, England facility for the manufacture of EXPAREL in two dedicated manufacturing suites. The Company contracted to purchase EXPAREL from Thermo Fisher, beginning with FDA approval of the suites, which occurred in May 2018. Commercial production began in February 2019. Under these agreements, the Company makes monthly base fee payments to Thermo Fisher. Unless earlier terminated by giving notice of up to three years (other than termination by the Company in the event of a material breach by Thermo Fisher), this agreement will expire in May 2028.

DePuy Synthes Sales, Inc.

In January 2017, the Company announced the initiation of a Co-Promotion Agreement, or the Agreement, with DePuy Synthes Sales, Inc., or DePuy Synthes, part of the Johnson & Johnson family of companies, to market and promote the use of
EXPAREL for orthopedic procedures in the U.S. DePuy Synthes field representatives, specializing in joint reconstruction, spine, sports medicine and trauma, collaborate with and supplement the Company's field teams by expanding the reach and frequency of EXPAREL education in the hospital surgical suite and ambulatory surgery center settings.

Under the five-year arrangement, DePuy Synthes is the exclusive third-party distributor during the term of the Agreement to promote and sell EXPAREL for operating room use for orthopedic and spine surgeries (including knee, hip, shoulder, sports and trauma surgeries) in the U.S. DePuy Synthes receives a tiered commission ranging from low single-digits to double-digits on sales of EXPAREL under the Agreement, subject to conditions, limitations and adjustments. The initial term of the Agreement commenced on January 24, 2017 and ends on December 31, 2021, with the option to extend the Agreement in additional 12-month increments upon mutual agreement of the parties, subject to certain conditions.

The Company and DePuy Synthes have mutual termination rights under the Agreement, subject to certain terms, conditions and advance notice requirements, provided that the Company or DePuy Synthes generally may not terminate the Agreement, without cause, within three years of the effective date of the Agreement. The Company also has additional unilateral termination rights under certain circumstances. The Agreement contains customary representations, warranties, covenants and confidentiality provisions, as well as mutual indemnification obligations. DePuy Synthes is also subject to certain obligations and restrictions, including required compliance with certain laws and regulations and the Company's policies, in connection with fulfilling their obligations under the Agreement.

Aratana Therapeutics, Inc.

On December 5, 2012, the Company entered into a worldwide license, development and commercialization agreement with Aratana Therapeutics, Inc., or Aratana. Under the agreement, the Company granted Aratana an exclusive royalty-bearing license, including the limited right to grant sublicenses, for the development and commercialization of the Company's bupivacaine liposome injectable suspension product for use in animals. Under the agreement, Aratana developed and obtained FDA approval for the use of the product in veterinary surgery to manage postsurgical pain. In connection with its entry into the license agreement, the Company received a one-time payment of $1.0 million. In December 2013, the Company received a $0.5 million milestone payment under the agreement. In June 2016, the Company recorded $1.0 million in milestone revenue for Aratana's filing of an FDA Administrative New Animal Drug Application, or ANADA, and in August 2016 recorded $1.0 million related to the FDA's approval of the ANADA. The Company is eligible to receive up to an additional aggregate $40.0 million upon the achievement of commercial milestones. Aratana is required to pay the Company a tiered double digit royalty on net sales made in the U.S. If the product is approved by foreign regulatory agencies for sale outside of the U.S., Aratana will be required to pay the Company a tiered double digit royalty on such net sales. Royalty rates will be reduced by a certain

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percentage upon the entry of a generic competitor for animal health indications into a jurisdiction or if Aratana must pay royalties to third parties under certain circumstances. Unless terminated earlier pursuant to its terms, the license agreement is effective until December 2027, after which Aratana has the option to extend the agreement for an additional five-year term, subject to certain requirements.

Aratana began purchasing bupivacaine liposome injectable suspension product in 2016, which they market under the trade name NOCITA® (a registered trademark of Aratana Therapeutics, Inc.) to serve animals.

CrossLink BioScience, LLC

In October 2013, the Company and CrossLink BioScience, LLC, or CrossLink, commenced a five-year arrangement for the promotion and sale of EXPAREL, pursuant to the terms of a Master Distributor Agreement. On June 30, 2016, the Company provided notice to CrossLink electing to terminate this agreement effective September 30, 2016. In connection with the termination of the agreement, the Company recorded a $7.1 million charge to selling, general and administrative expense in its consolidated statement of operations. There was nothing payable to CrossLink at December 31, 2018. $2.4 million was classified in accrued expenses at December 31, 2017.

Nuance Biotech Co. Ltd.

In June 2018, the Company entered into an agreement with Nuance Biotech Co. Ltd., or Nuance, a China-based specialty pharmaceutical company, to advance the development and commercialization of EXPAREL in China. Under the terms of the agreement, the Company agreed to be the sole supplier of EXPAREL to Nuance and has granted Nuance the exclusive rights to develop and commercialize EXPAREL in China. In June 2018, the Company recognized an upfront payment of $3.0 million since collaborative licensing revenue is recognized at the point in time when the license is provided and is not expected to substantively change. This payment was received in July 2018 and the Company is eligible to receive future milestone payments of up to $60.0 million that are triggered by filing for and securing regulatory approval(s) and annual sales in China exceeding certain levels. The Company is also entitled to tiered royalties as a percentage of net sales.

NOTE 17—RELATED PARTY TRANSACTIONS

The Company’s former Chief Medical Officer, Dr. Gary Patou, is a partner of MPM Asset Management LLC, or MPM, an investor in the Company. The Company incurred no consulting expenses with MPM or Dr. Patou in the years ended December 31, 2018 and 2017, and expenses of $0.1 million for the year ended December 31, 2016. At both December 31, 2018 and 2017, there were no amounts payable to MPM. The Company’s agreement with MPM expired on December 31, 2015, and the Company contracted with Dr. Patou directly for his services for the first six months of 2016.

In December 2012, the Company entered into a worldwide license, development and commercialization agreement with Aratana as discussed in Note 16, Commercial Partners and Other Agreements. MPM and its affiliates are holders of capital stock of Aratana. David Stack, the Company’s Chief Executive Officer and Chairman, was a managing director at MPM from 2005 through March 2017.

In April 2012, the Company entered into a consulting agreement with Dr. Gary Pace, a director of the Company. The Company recorded no expense under the consulting agreement in the years ended December 31, 2018 and 2017 and expenses of less than $0.1 million for the year ended December 31, 2016. In connection with the consulting agreement, Dr. Pace received an option to purchase 20,000 shares of common stock at an exercise price of $11.02 per share and an option to purchase 70,000 shares of common stock at an exercise price of $16.67 per share. At December 31, 2018 and 2017, there was nothing payable to Dr. Pace for consulting services.

NOTE 18—COMMITMENTS AND CONTINGENCIES

Leases

The Company leases its EXPAREL manufacturing, research and development, warehouse and DepoCyt(e) facilities in San Diego, California, and its corporate headquarters in Parsippany, New Jersey. Many of these leases provide

renewal options at the then-current market value. In addition, the Company has a lease for the use of Thermo Fisher's facility in Swindon, England embedded in the Thermo Fisher agreements and a portion of the monthly base fee has been allocated to the lease component based on a relative fair value basis.

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PACIRA PHARMACEUTICALS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

As of December 31, 2018, aggregate annual minimum payments due under the Company's lease obligations are as follows (in thousands):

Year	Aggregate Minimum Payments Due
2019	$ 8,140
2020	7,621
2021	5,295
2022	5,417
2023	5,543
2024 through 2028	14,329
Total	$ 46,345

Total rent expense, net of amortization of unfavorable lease obligations and tenant improvements, under all operating leases for the years ended December 31, 2018, 2017 and 2016 was $7.2 million, $7.5 million and $6.0 million, respectively. Deferred rent was $6.9 million at December 31, 2018 and $6.8 million at December 31, 2017.

Litigation

From time to time, the Company has been and may again become involved in legal proceedings arising in the ordinary course of its business, including those related to patents, product liability and government investigations. Except as described below, the Company is not presently a party to any legal proceedings which it believes to be material, and is not aware of any pending or threatened litigation against the Company which it believes could have a material adverse effect on its business, operating results, financial condition or cash flows.

In April 2015, the Company received a subpoena from the U.S. Department of Justice, U.S. Attorney's Office for the District of New Jersey, requiring the production of a broad range of documents pertaining to marketing and promotional practices related to EXPAREL. The Company is cooperating with the government's inquiry. The Company can make no assurances as to the time or resources that will need to be devoted to this inquiry or the impact, if any, of this inquiry or any proceedings on its business, financial condition, results of operations and cash flows.

Purchase Obligations

The Company has approximately $24.5 million of minimum, non-cancelable contractual commitments for contract manufacturing services as of December 31, 2018.

Other Commitments and Contingencies

The FDA, as a condition of EXPAREL approval, has required the Company to study EXPAREL in pediatric patients. The Company was granted a deferral for the required pediatric trials in all age groups for EXPAREL in the setting of wound infiltration and plans to conduct these pediatric trials as a post-marketing requirement, which was stated in the New Drug Application (NDA) approval letter for EXPAREL. The Company recently began activating a study site for an extended pharmacokinetic and safety study for local analgesia in children aged 6 to 17 undergoing cardiovascular or spine surgeries and is working with the FDA to define a program to study the administration of EXPAREL as a nerve block in the pediatric setting.

In addition to the initial $19.6 million purchase price for the Skyepharma Acquisition, the Company entered into an earn-out agreement with Skyepharma based on the Company reaching certain revenue milestones following the Skyepharma Acquisition. Pursuant to this agreement, the Company is required to pay Skyepharma milestone payments up to an aggregate of $62.0 million, of which $36.0 million are for milestones not yet met. The Company also agreed to pay certain earn-out payments based on a percentage of net sales of DepoBupivacaine products collected, including EXPAREL, for the term during which such sales were covered by a valid claim in certain patent rights related to EXPAREL and other biologics products. The last patents during which a valid claim existed expired

on September 18, 2018. Refer to Note 7, Goodwill, for further discussion.
Pursuant to an agreement with the Research Development Foundation, or RDF, the Company is required to pay RDF a low single-digit royalty on the collection of revenues from its DepoFoam-based products, for as long as certain patents assigned to the Company under the agreement remain valid. RDF has the right to terminate the agreement for an uncured material breach

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by the Company, in connection with its bankruptcy or insolvency or if it directly or indirectly opposes or disputes the validity of the assigned patent rights.

NOTE 19—SELECTED QUARTERLY FINANCIAL DATA (UNAUDITED)

The following tables present selected quarterly financial data for the years ended December 31, 2018 and 2017 (in thousands, except per share amounts):

	Three Months Ended			
	March 31, 2018	June 30, 2018	September 30, 2018	December 31, 2018
Total revenues	$74,607	$84,107	$83,448	$95,115
Cost of goods sold	22,885	20,916	19,065	23,979
Total operating expenses	81,544	77,566	79,400	82,852
Net income (loss)	(10,680)	2,564	(640)	8,285
Basic and diluted net income (loss) per common share	$(0.26)	$0.06	$(0.02)	$0.20

	Three Months Ended			
	March 31, 2017	June 30, 2017	September 30, 2017	December 31, 2017
Total revenues	$69,283	$70,934	$67,335	$79,078
Cost of goods sold	24,581	23,811	18,228	21,295
Total operating expenses	83,333	86,714	70,907	70,613
Net income (loss)	(19,866)	(19,743)	(7,597)	4,595
Basic and diluted net income (loss) per common share	$(0.52)	$(0.49)	$(0.19)	$0.11

For periods where the Company reported a net loss, no potentially dilutive securities were included in the computation of diluted net loss per share.