Restaurant Brands International Inc.
Form 10-Q
August 01, 2018
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

Form 10-Q

(Mark One)
QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2018

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to
Commission file number: 001-36786

RESTAURANT BRANDS INTERNATIONAL INC.
(Exact Name of Registrant as Specified in its Charter)

Canada	98-1202754
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)
226 Wyecroft Road Oakville, Ontario	L6K 3X7
(Address of Principal Executive Offices)	(Zip Code)

(905) 845-6511
(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 No
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," and "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act. (check one);

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

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

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

As of July 25, 2018, there were 250,012,986 common shares of the Registrant outstanding.

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PART I — Financial Information
Item 1. Financial Statements
RESTAURANT BRANDS INTERNATIONAL INC. AND SUBSIDIARIES
Condensed Consolidated Balance Sheets
(In millions of U.S. dollars, except share data)
(Unaudited)

	As of June 30, 2018	December 31, 2017
ASSETS		
Current assets:		
Cash and cash equivalents	$987.5	$ 1,097.4
Accounts and notes receivable, net of allowance of $17.4 and $16.4, respectively	441.8	488.8
Inventories, net	85.5	78.0
Prepaids and other current assets	116.1	85.4
Total current assets	1,630.9	1,749.6
Property and equipment, net of accumulated depreciation and amortization of $682.9 and $623.3, respectively	2,033.9	2,133.3
Intangible assets, net	10,736.4	11,062.2
Goodwill	5,619.9	5,782.3
Net investment in property leased to franchisees	61.8	71.3
Other assets, net	531.9	424.8
Total assets	$20,614.8	$ 21,223.5
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts and drafts payable	$474.4	$ 496.2
Other accrued liabilities	662.7	865.7
Gift card liability	102.5	214.9
Current portion of long term debt and capital leases	78.8	78.2
Total current liabilities	1,318.4	1,655.0
Term debt, net of current portion	11,776.0	11,800.9
Capital leases, net of current portion	231.1	243.8
Other liabilities, net	1,664.2	1,455.1
Deferred income taxes, net	1,400.8	1,508.1
Total liabilities	16,390.5	16,662.9
Shareholders' equity:		
Common shares, no par value; unlimited shares authorized at June 30, 2018 and December 31, 2017; 249,567,271 shares issued and outstanding at June 30, 2018; 243,899,476 shares issued and outstanding at December 31, 2017	2,116.4	2,051.5
Retained earnings	607.8	650.6
Accumulated other comprehensive income (loss)	(647.4)	(475.7)
Total Restaurant Brands International Inc. shareholders' equity	2,076.8	2,226.4
Noncontrolling interests	2,147.5	2,334.2
Total shareholders' equity	4,224.3	4,560.6
Total liabilities and shareholders' equity	$20,614.8	$ 21,223.5

See accompanying notes to condensed consolidated financial statements.

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RESTAURANT BRANDS INTERNATIONAL INC. AND SUBSIDIARIES
Condensed Consolidated Statements of Operations
(In millions of U.S. dollars, except per share data)
(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2018	2017	2018	2017
Revenues:				
Sales	$586.2	$602.1	$1,134.0	$1,152.5
Franchise and property revenues (Note 4)	757.2	530.6	1,463.2	980.8
Total revenues	1,343.4	1,132.7	2,597.2	2,133.3
Operating costs and expenses:				
Cost of sales	448.9	460.2	878.0	883.6
Franchise and property expenses	102.4	113.7	206.8	224.7
Selling, general and administrative expenses (Note 4)	317.6	96.7	618.9	218.6
(Income) loss from equity method investments	1.2	0.9	(13.1)	(4.8)
Other operating expenses (income), net	(29.4)	46.8	(16.7)	60.6
Total operating costs and expenses	840.7	718.3	1,673.9	1,382.7
Income from operations	502.7	414.4	923.3	750.6
Interest expense, net	129.8	128.0	269.9	239.4
Loss on early extinguishment of debt	—	—	—	20.4
Income before income taxes	372.9	286.4	653.4	490.8
Income tax expense	58.7	42.9	60.4	80.7
Net income	314.2	243.5	593.0	410.1
Net income attributable to noncontrolling interests (Note 11)	146.6	86.5	277.6	135.4
Preferred share dividends	—	67.5	—	135.0
Net income attributable to common shareholders	$167.6	$89.5	$315.4	$139.7
Earnings per common share				
Basic	$0.67	$0.38	$1.27	$0.59
Diluted	$0.66	$0.37	$1.25	$0.57
Weighted average shares outstanding				
Basic	249.3	235.8	247.6	235.2
Diluted	474.1	478.0	474.0	477.3
Cash dividends declared per common share	$0.45	$0.19	$0.90	$0.37

See accompanying notes to condensed consolidated financial statements.

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RESTAURANT BRANDS INTERNATIONAL INC. AND SUBSIDIARIES
Condensed Consolidated Statements of Comprehensive Income (Loss)
(In millions of U.S. dollars)
(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2018	2017	2018	2017
Net income	$314.2	$243.5	$593.0	$410.1
Foreign currency translation adjustment	(256.8)	355.4	(472.4)	461.2
Net change in fair value of net investment hedges, net of tax of $(29.3), $(48.8), $(37.9) and $(38.1)	113.5	(172.9)	116.0	(216.4)
Net change in fair value of cash flow hedges, net of tax of $0.3, $5.9, $(10.1) and $6.8	(0.7)	(16.5)	27.6	(19.1)
Amounts reclassified to earnings of cash flow hedges, net of tax of $(1.5), $(2.5), $(2.3) and $(3.8)	3.9	7.3	6.2	11.0
Gain (loss) recognized on defined benefit pension plans, net of tax of $0.0, $1.1, $0.0 and $1.4	—	0.6	0.2	0.3
Other comprehensive income (loss)	(140.1)	173.9	(322.4)	237.0
Comprehensive income (loss)	174.1	417.4	270.6	647.1
Comprehensive income (loss) attributable to noncontrolling interests	81.3	171.8	126.7	251.7
Comprehensive income attributable to preferred shareholders	—	67.5	—	135.0
Comprehensive income (loss) attributable to common shareholders	$92.8	$178.1	$143.9	$260.4

See accompanying notes to condensed consolidated financial statements.

RESTAURANT BRANDS INTERNATIONAL INC. AND SUBSIDIARIES
Condensed Consolidated Statements of Shareholders' Equity
(In millions of U.S. dollars, except shares)
(Unaudited)

	Issued Common Shares		Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Noncontrolling Interest	Total
	Shares	Amount				
Balances at December 31, 2017	243,899,476	$2,051.5	$650.6	$ (475.7)	$ 2,334.2	$4,560.6
Cumulative effect adjustment (Note 4)	—	—	(132.0)	—	(117.8)	(249.8)
Stock option exercises	5,469,375	29.0	—	—	—	29.0
Share-based compensation	—	26.5	—	—	—	26.5
Issuance of shares	126,065	6.6	—	—	—	6.6
Dividends declared on common shares	—	—	(224.3)	—	—	(224.3)
Dividend equivalents declared on restricted stock units	—	1.9	(1.9)	—	—	—
Distributions declared by Partnership on Partnership exchangeable units (Note 11)	—	—	—	—	(195.9)	(195.9)
Exchange of Partnership exchangeable units for RBI common shares	72,355	0.9	—	(0.2)	(0.7)	—
Restaurant VIE contributions (distributions)	—	—	—	—	1.0	1.0
Net income	—	—	315.4	—	277.6	593.0
Other comprehensive income (loss)	—	—	—	(171.5)	(150.9)	(322.4)
Balances at June 30, 2018	249,567,271	$2,116.4	$607.8	$ (647.4)	$ 2,147.5	$4,224.3

See accompanying notes to condensed consolidated financial statements.

RESTAURANT BRANDS INTERNATIONAL INC. AND SUBSIDIARIES
Condensed Consolidated Statements of Cash Flows
(In millions of U.S. dollars)
(Unaudited)

	Six Months Ended June 30,	
	2018	2017
Cash flows from operating activities:		
Net income	$593.0	$410.1
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	92.6	88.7
Premiums paid and non-cash loss on early extinguishment of debt	—	17.9
Amortization of deferred financing costs and debt issuance discount	14.5	16.7
(Income) loss from equity method investments	(13.1)	(4.8)
Loss (gain) on remeasurement of foreign denominated transactions	(16.2)	47.1
Net (gains) losses on derivatives	(14.8)	14.9
Share-based compensation expense	26.6	27.2
Deferred income taxes	(58.1)	22.4
Other	4.3	9.8
Changes in current assets and liabilities, excluding acquisitions and dispositions:		
Accounts and notes receivable	36.2	27.4
Inventories and prepaids and other current assets	(15.6)	(4.9)
Accounts and drafts payable	(11.4)	(5.4)
Other accrued liabilities and gift card liability	(347.4)	(164.2)
Other long-term assets and liabilities	(3.2)	(12.9)
Net cash provided by operating activities	287.4	490.0
Cash flows from investing activities:		
Payments for property and equipment	(21.6)	(11.7)
Proceeds from disposal of assets, restaurant closures, and refranchisings	3.4	9.6
Net payment for purchase of Popeyes, net of cash acquired	—	(1,635.9)
Return of investment on direct financing leases	8.3	7.8
Settlement/sale of derivatives, net	11.2	772.0
Other investing activities, net	0.2	0.3
Net cash provided by (used for) investing activities	1.5	(857.9)
Cash flows from financing activities:		
Proceeds from issuance of long-term debt	—	3,050.0
Repayments of long-term debt and capital leases	(43.3)	(377.7)
Payment of financing costs	—	(47.0)
Payment of dividends on common and preferred shares and distributions on Partnership exchangeable units	(307.0)	(296.6)
Payments in connection with redemption of preferred shares	(60.1)	—
Proceeds from stock option exercises	29.0	12.3
Other financing activities, net	(1.8)	(2.3)
Net cash (used for) provided by financing activities	(383.2)	2,338.7
Effect of exchange rates on cash and cash equivalents	(15.6)	13.3
Increase (decrease) in cash and cash equivalents	(109.9)	1,984.1
Cash and cash equivalents at beginning of period	1,097.4	1,475.8
Cash and cash equivalents at end of period	$987.5	$3,459.9
Supplemental cash flow disclosures:		

Interest paid	$273.6	$205.6
Income taxes paid	$374.0	$116.9

See accompanying notes to condensed consolidated financial statements.

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RESTAURANT BRANDS INTERNATIONAL INC. AND SUBSIDIARIES
Notes to Condensed Consolidated Financial Statements
(Unaudited)

Note 1. Description of Business and Organization

Restaurant Brands International Inc. (the "Company", "RBI", "we", "us" or "our") was formed on August 25, 2014 and continued under the laws of Canada. The Company serves as the sole general partner of Restaurant Brands International Limited Partnership ("Partnership"). We franchise and operate quick service restaurants serving premium coffee and other beverage and food products under the Tim Hortons® brand ("Tim Hortons" or "TH"), fast food hamburgers principally under the Burger King® brand ("Burger King" or "BK"), and chicken under the Popeyes® brand ("Popeyes" or "PLK"). We are one of the world's largest quick service restaurant, or QSR, companies as measured by total number of restaurants. As of June 30, 2018, we franchised or owned 4,794 Tim Hortons restaurants, 17,022 Burger King restaurants, and 2,975 Popeyes restaurants, for a total of 24,791 restaurants, and operate in more than 100 countries and U.S. territories. Approximately 100% of current system-wide restaurants are franchised.

All references to "$" or "dollars" are to the currency of the United States unless otherwise indicated. All references to Canadian dollars or C$ are to the currency of Canada unless otherwise indicated.

Note 2. Basis of Presentation and Consolidation

We have prepared the accompanying unaudited condensed consolidated financial statements (the "Financial Statements") in accordance with the rules and regulations of the Securities and Exchange Commission (the "SEC") for interim financial information. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America ("U.S. GAAP") for complete financial statements. Therefore, the Financial Statements should be read in conjunction with the audited consolidated financial statements contained in our Annual Report on Form 10-K filed with the SEC and Canadian securities regulatory authorities on February 23, 2018.

The Financial Statements include our accounts and the accounts of entities in which we have a controlling financial interest, the usual condition of which is ownership of a majority voting interest. All material intercompany balances and transactions have been eliminated in consolidation. Investments in other affiliates that are owned 50% or less where we have significant influence are accounted for by the equity method.

We are the sole general partner of Partnership and, as such we have the exclusive right, power and authority to manage, control, administer and operate the business and affairs and to make decisions regarding the undertaking and business of Partnership, subject to the terms of the amended and restated limited partnership agreement of Partnership (the "partnership agreement") and applicable laws. As a result, we consolidate the results of Partnership and record a noncontrolling interest in our consolidated balance sheets and statements of operations with respect to the remaining economic interest in Partnership we do not hold.

We also consider for consolidation entities in which we have certain interests, where the controlling financial interest may be achieved through arrangements that do not involve voting interests. Such an entity, known as a variable interest entity ("VIE"), is required to be consolidated by its primary beneficiary.

Tim Hortons has historically entered into certain arrangements in which an operator acquires the right to operate a restaurant, but Tim Hortons owns the restaurant's assets. We perform an analysis to determine if the legal entity in which operations are conducted is a VIE and consolidate a VIE entity if we also determine Tim Hortons is the entity's primary beneficiary ("Restaurant VIEs"). As of June 30, 2018 and December 31, 2017, we determined that we are the primary beneficiary of 21 and 31 Restaurant VIEs, respectively. As Tim Hortons, Burger King, and Popeyes franchise and master franchise arrangements provide the franchise and master franchise entities the power to direct the activities that most significantly impact their economic performance, we do not consider ourselves the primary beneficiary of any such entity that might be a VIE.

In the opinion of management, all adjustments (consisting of normal recurring adjustments) necessary for a fair presentation have been included in the Financial Statements. The results for interim periods are not necessarily indicative of the results that may be expected for any other interim period or for the full year.

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The preparation of consolidated financial statements in conformity with U.S. GAAP and related rules and regulations of the SEC requires our management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, and the related disclosure of contingent assets and liabilities. Actual results could differ from these estimates.

Certain prior year amounts in the accompanying Financial Statements and notes to the Financial Statements have been reclassified in order to be comparable with the current year classifications. These consist of the December 31, 2017 reclassification of Advertising fund restricted assets to Cash and cash equivalents, Accounts and notes receivable, net and Prepaids and other current assets and the reclassification of Advertising fund liabilities to Accounts and drafts payable and Other accrued liabilities as detailed below (in millions). These reclassifications had no effect on previously reported net income.

	December 31, 2017 As Reported	Reclassification	December 31, 2017 As Adjusted
Current assets:			
Cash and cash equivalents	$ 1,073.4	$ 24.0	$ 1,097.4
Accounts and notes receivable, net	455.9	32.9	488.8
Inventories, net	78.0	—	78.0
Advertising fund restricted assets	83.3	(83.3)	—
Prepaids and other current assets	59.0	26.4	85.4
Total current assets	$ 1,749.6	$ —	$ 1,749.6
Current liabilities:			
Accounts and drafts payable	$ 412.9	$ 83.3	$ 496.2
Other accrued liabilities	838.2	27.5	865.7
Gift card liability	214.9	—	214.9
Advertising fund liabilities	110.8	(110.8)	—
Current portion of long term debt and capital leases	78.2	—	78.2
Total current liabilities	$ 1,655.0	$ —	$ 1,655.0

Note 3. New Accounting Pronouncements

Revenue Recognition – In May 2014, the Financial Accounting Standards Board (the “FASB”) issued a new single comprehensive model for entities to use in accounting for revenue arising from contracts with customers. We adopted this new guidance on January 1, 2018. See Note 4, Revenue Recognition, for further information about our transition to this new revenue recognition model using the modified retrospective transition method.

Lease Accounting – In February 2016, the FASB issued new guidance on leases. The new guidance requires lessees to recognize on the balance sheet the assets and liabilities for the rights and obligations created by finance and operating leases with lease terms of more than 12 months, amends various other aspects of accounting for leases by lessees and lessors, and requires enhanced disclosures. The new guidance is effective commencing in 2019 and requires either a modified retrospective transition approach with application in all comparative periods presented, or an alternative transition method, which permits a company to use its effective date as the date of initial application without restating comparative period financial statements. The new guidance also provides several practical expedients and policies that companies may elect under either transition method. We currently expect to apply the alternative transition method and elect the package of practical expedients under which we will not reassess the classification of our existing leases, reevaluate whether any expired or existing contracts are or contain leases or reassess initial direct costs under the new guidance. We do not expect to elect the practical expedient that permits a reassessment of lease terms for existing leases and are continuing to evaluate other practical expedients and elections specified in the new guidance.

We have commenced an analysis of the impact of the new lease guidance and developed a comprehensive plan for our implementation of the new guidance. The project plan includes analyzing the impact of the new guidance on our current lease contracts, reviewing the completeness of our existing lease portfolio, comparing our accounting policies under current accounting guidance to the new accounting guidance and identifying potential differences from applying the requirements of

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the new guidance to our lease contracts. Under current accounting guidance for leases, we do not recognize an asset or liability created by operating leases where we are the lessee. We expect a material increase to our assets and liabilities on our consolidated balance sheet as a result of recognizing assets and liabilities for operating leases where we are the lessee on the date of initial application of the new guidance. We are continuing to evaluate the impact of the new guidance on capital leases and direct finance leases. We are also continuing to evaluate the impact that adoption of this guidance will have on our consolidated statements of operations. We do not expect the adoption of this new guidance to have a material impact on the amount or timing of our cash flows and liquidity.

Goodwill Impairment – In January 2017, the FASB issued guidance to simplify how an entity measures goodwill impairment by removing the second step of the two-step quantitative goodwill impairment test. An entity will no longer be required to perform a hypothetical purchase price allocation to measure goodwill impairment. Instead, impairment will be measured at the amount by which the carrying value exceeds the fair value of a reporting unit; however, the loss recognized should not exceed the total amount of goodwill allocated to that reporting unit. The amendment requires prospective adoption and is effective commencing in 2020 with early adoption permitted.

Hedge Accounting – In August 2017, the FASB issued guidance to improve the transparency and understandability of information conveyed to financial statement users about an entity's risk management activities and to simplify the application of hedge accounting by preparers. We adopted this guidance on January 1, 2018 (the “Adoption Date”). The new guidance eliminates the requirement to separately measure and report hedge ineffectiveness for cash flow and net investment hedges that are deemed effective. Most notably, for our cross-currency swaps designated as net investment hedges, the new guidance permits the exclusion of the interest component (the “Excluded Component”) from the accounting hedge without affecting net investment hedge designation. The initial value of the Excluded Component may be recognized in earnings on a systematic and rational basis over the life of the derivative instrument. Subsequent to the Adoption Date, we changed the method of assessing effectiveness for net investment hedges using derivatives from the forward method to the spot method. We de-designated the cross currency-swaps and re-designated them as of March 15, 2018 (the "Re-designation Date"). As a result of adopting the new guidance and the re-designation of our cross- currency-swaps, we will recognize a benefit from the amortization of the initial value of the Excluded Component as a component of Interest expense, net in our condensed consolidated statements of operations rather than as a component of other comprehensive income. All changes in fair value of the instruments related to currency fluctuations will continue to be recognized within other comprehensive income.

The impact of adoption did not have a material effect on our Financial Statements as of the Adoption Date. We recorded a $19.9 million net benefit to Interest expense, net during the three months ended June 30, 2018 and a $23.5 million net benefit to Interest expense, net from the Re-designation Date through June 30, 2018 in our condensed consolidated statements of operations for the amortization of the initial value of the Excluded Component, as described above. We believe the new guidance better portrays the economic results of our risk management activities and net investment hedges in our Financial Statements.

Reclassification of Certain Tax Effects – In February 2018, the FASB issued guidance which allows a reclassification from accumulated other comprehensive income to retained earnings for the tax effects of certain items within accumulated other comprehensive income. The amendment is effective commencing in 2019 with early adoption permitted. We are currently evaluating the impact that the adoption of this new guidance will have on our Financial Statements.

Share-based payment arrangements with nonemployees – In June 2018, the FASB issued guidance which simplifies the accounting for share-based payments granted to nonemployees for goods and services. Most of the guidance on such payments to nonemployees would be aligned with the requirements for share-based payments granted to employees. The amendment is effective commencing in 2019 with early adoption permitted. We are currently evaluating the impact that the adoption of this new guidance will have on our Financial Statements.

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Note 4. Revenue Recognition
Revenue from Contracts with Customers
We transitioned to FASB Accounting Standards Codification (“ASC”) Topic 606, Revenue From Contracts with Customers (“ASC 606”), from ASC Topic 605, Revenue Recognition and ASC Subtopic 952-605, Franchisors - Revenue Recognition (together, the “Previous Standards”) on January 1, 2018 using the modified retrospective transition method. Our Financial Statements reflect the application of ASC 606 guidance beginning in 2018, while our consolidated financial statements for prior periods were prepared under the guidance of the Previous Standards. The $249.8 million cumulative effect of our transition to ASC 606 is reflected as an adjustment to January 1, 2018 Shareholders' equity.
Our transition to ASC 606 represents a change in accounting principle. ASC 606 eliminates industry-specific guidance and provides a single revenue recognition model for recognizing revenue from contracts with customers. The core principle of ASC 606 is that a reporting entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the reporting entity expects to be entitled for the exchange of those goods or services.
Revenue Recognition Significant Accounting Policies under ASC 606
Our revenues are comprised of sales and franchise and property revenues, which are detailed as follows:
Sales
Sales consist primarily of supply chain sales, which represent sales of products, supplies and restaurant equipment to franchisees, as well as sales to retailers. Orders placed by customers specify the goods to be delivered and transaction prices for supply chain sales. Revenue is recognized upon transfer of control over ordered items, generally upon delivery to the customer, which is when the customer obtains physical possession of the goods, legal title is transferred, the customer has all risks and rewards of ownership and an obligation to pay for the goods is created. Shipping and handling costs associated with outbound freight for supply chain sales are accounted for as fulfillment costs and classified as cost of sales.
Commencing on January 1, 2018, we classify all sales of restaurant equipment to franchisees as Sales and related cost of equipment sold as Cost of sales. In periods prior to January 1, 2018, we classified sales of restaurant equipment at establishment of a restaurant and in connection with renewal or renovation as Franchise and property revenues and related costs as Franchise and property expense.
To a much lesser extent, sales also include Company restaurant sales (including Restaurant VIEs), which consist of sales to restaurant guests. Revenue from Company restaurant sales is recognized at the point of sale. Taxes assessed by a governmental authority that we collect are excluded from revenue.
Franchise and Property Revenues
Franchise revenues
Franchise revenues consist primarily of royalties, advertising fund contributions, initial and renewal franchise fees and upfront fees from development agreements and master franchise and development agreements (“MFDAs”). Our performance obligations under franchise agreements consist of (a) a franchise license, including a license to use one of our brands and, where our subsidiaries manage an advertising fund, advertising and promotion management, (b) pre-opening services, such as training and inspections, and (c) ongoing services, such as development of training materials and menu items and restaurant monitoring and inspections. These performance obligations are highly interrelated, so we do not consider them to be individually distinct and therefore account for them under ASC 606 as a single performance obligation, which is satisfied by providing a right to use our intellectual property over the term of each franchise agreement.
Royalties, including franchisee contributions to advertising funds managed by our subsidiaries, are calculated as a percentage of franchise restaurant sales over the term of the franchise agreement. Under our franchise agreements, advertising contributions paid by franchisees must be spent on advertising, product development, marketing and related activities. Initial and renewal franchise fees are payable by the franchisee upon a new restaurant opening or renewal of an existing franchise agreement. Our franchise agreement royalties, inclusive of advertising fund contributions, represent sales-based royalties that are related entirely to our performance obligation under the franchise agreement and are recognized as franchise sales occur. Additionally, under ASC 606, initial and renewal

franchise fees are recognized as revenue on a straight-line basis over the term of the respective agreement. Under the Previous Standards, initial franchise fees were recognized as revenue when the related restaurant commenced operations and our completion of all material services and conditions. Renewal franchise fees were recognized as revenue upon execution of a new franchise agreement. Our performance obligation under development agreements other than MFDAs generally consists of an obligation to grant exclusive development rights over a stated term. These development rights are not distinct from franchise agreements, so upfront fees paid by franchisees for exclusive development rights are deferred and apportioned to each franchise restaurant opened by the franchisee. The pro rata amount apportioned to each restaurant is accounted for as an initial franchise fee.

We have a distinct performance obligation under our MFDAs to grant subfranchising rights over a stated term. Under the terms of MFDAs, we typically either receive an upfront fee paid in cash and/or receive noncash consideration in the form of an equity interest in the master franchisee or an affiliate of the master franchisee. We previously accounted for noncash consideration as a nonmonetary exchange and did not record revenue or a basis in the equity interest received in arrangements where we received noncash consideration. These transactions now fall within the scope of ASC 606, which requires us to record investments in the applicable equity method investee and recognize revenue in an amount equal to the fair value of the equity interest received. Upfront fees from master franchisees, including the fair value of noncash consideration, are deferred and amortized over the MFDA term on a straight-line basis. We may recognize unamortized upfront fees when a contract with a franchisee or master franchisee is modified and is accounted for as a termination of the existing contract.

The portion of gift cards sold to customers which are never redeemed is commonly referred to as gift card breakage. Under ASC 606, we recognize gift card breakage income proportionately as each gift card is redeemed using an estimated breakage rate based on our historical experience. Under the Previous Standards, we recognized gift card breakage income for each gift card's remaining balance when redemption of that balance was deemed remote.

Property Revenues

Property revenues are accounted for in accordance with applicable accounting guidance for leases and are excluded from the scope of ASC 606. See Note 2, Significant Accounting Policies, to our consolidated financial statements included in our Annual Report on Form 10-K for the fiscal year ended December 31, 2017 for our property revenue accounting policies.

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Contract Liabilities

Contract liabilities consist of deferred revenue resulting from initial and renewal franchise fees paid by franchisees, as well as upfront fees paid by master franchisees, which are generally recognized on a straight-line basis over the term of the underlying agreement. We classify these contract liabilities as Other liabilities, net in our condensed consolidated balance sheets. The following table reflects the change in contract liabilities between the date of adoption (January 1, 2018) and June 30, 2018 (in millions):

	Contract Liabilities
Balance at January 1, 2018	$ 455.0
Revenue recognized that was included in the contract liability balance at the beginning of the year	(30.7)
Increase, excluding amounts recognized as revenue during the period	40.6
Impact of foreign currency translation	(9.9)
Balance at June 30, 2018	$ 455.0

The following table illustrates estimated revenues expected to be recognized in the future related to performance obligations that are unsatisfied (or partially unsatisfied) as of June 30, 2018 (in millions):

Contract liabilities expected to be recognized in	Amount
Remainder of 2018	$ 17.6
2019	34.2
2020	33.5
2021	32.8
2022	32.0
Thereafter	304.9
Total	$ 455.0

Disaggregation of Total Revenues

Total revenues consist of the following (in millions):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2018	2017	2018	2017
Sales	$ 586.2	$ 602.1	$ 1,134.0	$ 1,152.5
Royalties	543.9	308.7	1,054.3	550.7
Property revenues	190.5	189.3	368.3	364.3
Franchise fees and other revenue	22.8	32.6	40.6	65.8
Total revenues	$ 1,343.4	$ 1,132.7	$ 2,597.2	$ 2,133.3

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Financial Statement Impact of Transition to ASC 606

As noted above, we transitioned to ASC 606 using the modified retrospective method on January 1, 2018. The cumulative effect of this transition to applicable contracts with customers that were not completed as of January 1, 2018 was recorded as an adjustment to Shareholders' equity as of this date. As a result of applying the modified retrospective method to transition to ASC 606, the following adjustments were made to the consolidated balance sheet as of January 1, 2018 (in millions):

	As Reported December 31, 2017	Total Adjustments	Adjusted January 1, 2018
ASSETS			
Current assets:			
Cash and cash equivalents	$1,097.4	$ —	$1,097.4
Accounts and notes receivable, net	488.8	—	488.8
Inventories, net	78.0	—	78.0
Prepaids and other current assets	85.4	(23.0)	62.4
Total current assets	1,749.6	(23.0)	1,726.6
Property and equipment, net	2,133.3	—	2,133.3
Intangible assets, net	11,062.2	—	11,062.2
Goodwill	5,782.3	—	5,782.3
Net investment in property leased to franchisees	71.3	—	71.3
Other assets, net	424.8	106.6	531.4
Total assets	$21,223.5	$ 83.6	$21,307.1
LIABILITIES AND SHAREHOLDERS’ EQUITY			
Current liabilities:			
Accounts and drafts payable	$496.2	$ —	$496.2
Other accrued liabilities	865.7	8.9	874.6
Gift card liability	214.9	(43.0)	171.9
Current portion of long term debt and capital leases	78.2	—	78.2
Total current liabilities	1,655.0	(34.1)	1,620.9
Term debt, net of current portion	11,800.9	—	11,800.9
Capital leases, net of current portion	243.8	—	243.8
Other liabilities, net	1,455.1	425.7	1,880.8
Deferred income taxes, net	1,508.1	(58.2)	1,449.9
Total liabilities	16,662.9	333.4	16,996.3
Shareholders’ equity:			
Common shares	2,051.5	—	2,051.5
Retained earnings	650.6	(132.0)	518.6
Accumulated other comprehensive income (loss)	(475.7)	—	(475.7)
Total RBI shareholders’ equity	2,226.4	(132.0)	2,094.4
Noncontrolling interests	2,334.2	(117.8)	2,216.4
Total shareholders’ equity	4,560.6	(249.8)	4,310.8
Total liabilities and shareholders’ equity	$21,223.5	$ 83.6	$21,307.1

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Franchise Fees

The cumulative adjustment for franchise fees consists of the following:

- A $320.7 million increase in Other liabilities, net for the cumulative reversal and deferral of previously recognized franchise fees related to franchise agreements in effect at January 1, 2018 that were entered into subsequent to the acquisitions of BK in 2010, TH in 2014 and PLK in 2017 (net of the cumulative revenue attributable for the period through January 1, 2018), with a corresponding decrease to Shareholders' equity.
- A $106.6 million increase in Other assets, net for the previously unrecognized value of equity interests received in connection with MFDA arrangements. This increase resulted in a corresponding increase in Other liabilities, net of $105.0 million and an adjustment to Shareholders' equity of $1.6 million for the cumulative effect of revenue attributable for the period between the inception of each such arrangement and January 1, 2018.
- A $67.1 million decrease to Deferred income taxes, net for the tax effects of the two adjustments noted above, with a corresponding increase to Shareholders' equity.

Advertising Funds

The cumulative adjustment for advertising funds reflects the recognition of cumulative advertising expenditures temporarily in excess of cumulative advertising fund contributions as of January 1, 2018, which is reflected as a $23.0 million decrease in Prepaids and other current assets and a $23.0 million decrease to Shareholders' equity.

Gift Card Breakage

The adjustment for gift card breakage reflects the impact of the change to recognize gift card breakage proportionately as gift card balances are used rather than when it is deemed remote that the unused gift card balance would be redeemed, as done under the Previous Standards. The cumulative effect of applying ASC 606 accounting to gift card balances outstanding at January 1, 2018 is reflected as a $43.0 million decrease in Gift card liability, an $8.9 million increase in Other accrued liabilities, an $8.9 million increase in Deferred income taxes, net and a $25.2 million increase in January 1, 2018 Shareholders' equity.

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Comparison to Amounts if Previous Standards Had Been in Effect

The following tables reflect the impact of adoption of ASC 606 on our condensed consolidated statements of operations for the three and six months ended June 30, 2018 and cash flows from operating activities for the six months ended June 30, 2018 and our condensed consolidated balance sheet as of June 30, 2018 and the amounts as if the Previous Standards were in effect ("Amounts Under Previous Standards") (in millions):

Condensed Consolidated Statement of Operations for the three and six months ended June 30, 2018

	Three Months Ended June 30, 2018			Six Months Ended June 30, 2018		
	As Reported	Total Adjustments	Amounts Under Previous Standards	As Reported	Total Adjustments	Amounts Under Previous Standards
Revenues:						
Sales	$586.2	$ —	$ 586.2	$1,134.0	$ —	$1,134.0
Franchise and property revenues	757.2	(199.1)	558.1	1,463.2	(381.1)	1,082.1
Total revenues	1,343.4	(199.1)	1,144.3	2,597.2	(381.1)	2,216.1
Operating costs and expenses:						
Cost of sales	448.9	—	448.9	878.0	—	878.0
Franchise and property expenses	102.4	—	102.4	206.8	(0.2)	206.6
Selling, general and administrative expenses	317.6	(200.1)	117.5	618.9	(390.6)	228.3
(Income) loss from equity method investments	1.2	(3.6)	(2.4)	(13.1)	(3.6)	(16.7)
Other operating expenses (income), net	(29.4)	—	(29.4)	(16.7)	—	(16.7)
Total operating costs and expenses	840.7	(203.7)	637.0	1,673.9	(394.4)	1,279.5
Income from operations	502.7	4.6	507.3	923.3	13.3	936.6
Interest expense, net	129.8	0.7	130.5	269.9	1.2	271.1
Income before income taxes	372.9	3.9	376.8	653.4	12.1	665.5
Income tax expense	58.7	1.1	59.8	60.4	3.2	63.6
Net income	314.2	2.8	317.0	593.0	8.9	601.9
Net income attributable to noncontrolling interests	146.6	1.3	147.9	277.6	4.2	281.8
Net income attributable to common shareholders	$167.6	$ 1.5	$ 169.1	$315.4	$ 4.7	$320.1
Earnings per common share:						
Basic	$0.67		$ 0.68	$1.27		$1.29
Diluted	$0.66		$ 0.67	$1.25		$1.27

The following summarizes the adjustments to our condensed consolidated statement of operations for the three and six months ended June 30, 2018 to reflect our condensed consolidated statement of operations as if we had continued to recognize revenue under the Previous Standards:

- As described above, our transition to ASC 606 resulted in the deferral of franchise fees, recognition of franchise fees in connection with MFDAs where we received an equity interest in the equity method investee, and a change in the timing of recognizing gift card breakage income. The adjustments for the three and six months ended June 30, 2018 to reflect the recognition of this revenue as if the Previous Standards were in effect consists of a $1.1 million and $5.0 million increase in Franchise and property revenue, respectively, and a $1.3 million and $2.4 million increase in Income tax expense, respectively.
- The adjustments to (income) loss from equity method investments for the three and six months ended June 30, 2018 reflect the amount of losses from equity method investments we would not have recognized if the Previous Standards were in effect. There is no tax impact related to these adjustments.
- As described above, under the Previous Standards our statement of operations did not reflect gross presentations of advertising fund contributions and expenses. Our transition to ASC 606 requires the presentation of advertising fund

contributions and advertising fund expenses on a gross basis. The adjustments for the three and six months ended June 30, 2018 to reflect advertising fund contributions and expenses as if the Previous Standards were in effect consist of a

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$200.2 million and $386.1 million decrease in Franchise and property revenues, respectively, a $0.0 million and $0.2 million decrease in Franchise and property expenses, respectively, a $200.1 million and $390.6 million decrease in Selling, general and administrative expenses, respectively, a $0.7 million and $1.2 million increase in Interest expense, net, respectively, and a $0.2 million decrease and $0.8 million increase in Income tax expense, respectively.

Condensed Consolidated Statement of Cash Flows for the six months ended June 30, 2018

The transition to ASC 606 had no net impact on our cash provided by operating activities and no impact on our cash provided by investing activities or cash used for financing activities during the six months ended June 30, 2018.

	As Reported	Total Adjustments	Amounts Under Previous Standards
Cash flows from operating activities:			
Net income	$ 593.0	$ 8.9	$ 601.9
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	92.6	—	92.6
Amortization of deferred financing costs and debt issuance discount	14.5	—	14.5
(Income) loss from equity method investments	(13.1)	(3.6)	(16.7)
Loss (gain) on remeasurement of foreign denominated transactions	(16.2)	—	(16.2)
Net losses on derivatives	(14.8)	—	(14.8)
Share-based compensation expense	26.6	—	26.6
Deferred income taxes	(58.1)	3.2	(54.9)
Other	4.3	—	4.3
Changes in current assets and liabilities, excluding acquisitions and dispositions:			
Accounts and notes receivable	36.2	—	36.2
Inventories and prepaids and other current assets	(15.6)	(4.4)	(20.0)
Accounts and drafts payable	(11.4)	3.8	(7.6)
Other accrued liabilities and gift card liability	(347.4)	(2.3)	(349.7)
Other long-term assets and liabilities	(3.2)	(5.6)	(8.8)
Net cash provided by operating activities	$ 287.4	$ —	$ 287.4

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Condensed Consolidated Balance Sheet

	As Reported June 30, 2018	Total Adjustments	Amounts Under Previous Standards
ASSETS			
Current assets:			
Cash and cash equivalents	$987.5	$ —	$987.5
Accounts and notes receivable, net	441.8	—	441.8
Inventories, net	85.5	—	85.5
Prepaids and other current assets	116.1	27.4	143.5
Total current assets	1,630.9	27.4	1,658.3
Property and equipment, net	2,033.9	—	2,033.9
Intangible assets, net	10,736.4	—	10,736.4
Goodwill	5,619.9	—	5,619.9
Net investment in property leased to franchisees	61.8	—	61.8
Other assets, net	531.9	(103.0)	428.9
Total assets	$20,614.8	$ (75.6)	$20,539.2
LIABILITIES AND SHAREHOLDERS' EQUITY			
Current liabilities:			
Accounts and drafts payable	$474.4	$ 3.8	$478.2
Other accrued liabilities	662.7	(11.8)	650.9
Gift card liability	102.5	43.6	146.1
Current portion of long term debt and capital leases	78.8	—	78.8
Total current liabilities	1,318.4	35.6	1,354.0
Term debt, net of current portion	11,776.0	—	11,776.0
Capital leases, net of current portion	231.1	—	231.1
Other liabilities, net	1,664.2	(431.3)	1,232.9
Deferred income taxes, net	1,400.8	61.4	1,462.2
Total liabilities	16,390.5	(334.3)	16,056.2
Shareholders' equity:			
Common shares	2,116.4	—	2,116.4
Retained earnings	607.8	138.2	746.0
Accumulated other comprehensive income (loss)	(647.4)	—	(647.4)
Total RBI shareholders' equity	2,076.8	138.2	2,215.0
Noncontrolling interests	2,147.5	120.5	2,268.0
Total shareholders' equity	4,224.3	258.7	4,483.0
Total liabilities and shareholders' equity	$20,614.8	$ (75.6)	$20,539.2

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Note 5. Earnings per Share

An economic interest in Partnership common equity is held by the holders of Class B exchangeable limited partnership units (the “Partnership exchangeable units”), which is reflected as a noncontrolling interest in our equity. See Note 11, Shareholders’ Equity.

Basic and diluted earnings per share is computed using the weighted average number of shares outstanding for the period. We apply the treasury stock method to determine the dilutive weighted average common shares represented by Partnership exchangeable units and outstanding equity awards, unless the effect of their inclusion is anti-dilutive. The diluted earnings per share calculation assumes conversion of 100% of the Partnership exchangeable units under the “if converted” method. Accordingly, the numerator is also adjusted to include the earnings allocated to the holders of noncontrolling interests.

The following table summarizes the basic and diluted earnings per share calculations (in millions, except per share amounts):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2018	2017	2018	2017
Numerator:				
Net income attributable to common shareholders - basic	$167.6	$89.5	$315.4	$139.7
Add: Net income attributable to noncontrolling interests	146.4	86.1	277.2	134.6
Net income available to common shareholders and noncontrolling interests - diluted	$314.0	$175.6	$592.6	$274.3
Denominator:				
Weighted average common shares - basic	249.3	235.8	247.6	235.2
Exchange of noncontrolling interests for common shares (Note 11)	217.6	226.9	217.7	226.9
Effect of other dilutive securities	7.2	15.3	8.7	15.2
Weighted average common shares - diluted	474.1	478.0	474.0	477.3
Basic earnings per share	$0.67	$0.38	$1.27	$0.59
Diluted earnings per share	$0.66	$0.37	$1.25	$0.57
Anti-dilutive securities outstanding	5.8	4.2	5.8	4.2

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Note 6. Intangible Assets, net and Goodwill

Intangible assets, net and goodwill consist of the following (in millions):

	As of					
	June 30, 2018			December 31, 2017		
	Gross	Accumulated Amortization	Net	Gross	Accumulated Amortization	Net
Identifiable assets subject to amortization:						