Square, Inc.
Form 10-Q
May 02, 2018
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)
ý QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended March 31, 2018
OR
o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from ________ to ________
Commission File Number: 001-37622

Square, Inc.
(Exact name of registrant as specified in its charter)

Delaware	80-0429876
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)

1455 Market Street, Suite 600
San Francisco, CA 94103
(Address of principal executive offices, including zip code)
(415) 375-3176
(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 ý No o
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ý No o
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See definitions of “large accelerated filer,” “accelerated filer,” “smaller reporting company,” and “emerging growth company” in Rule 12b-2 of the Exchange Act.
Large accelerated filer ý Accelerated filer o Non-accelerated filer o (Do not check if smaller reporting company) Smaller reporting company o Emerging growth company o

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

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

As of April 30, 2018, the number of shares of the registrant's Class A common stock outstanding was 289,951,143 and the number of shares of the registrant's Class B common stock outstanding was 110,743,787.

TABLE OF CONTENTS

SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, that involve substantial risks and uncertainties. Forward-looking statements generally relate to future events or our future financial or operating performance. In some cases, you can identify forward-looking statements because they contain words such as “may,” “will,” “appears,” “should,” “expects,” “plans,” “anticipates,” “could,” “intends,” “target,” “projects,” “c “believes,” “estimates,” “predicts,” “potential,” or “continue,” or the negative of these words or other similar terms or expressions that concern our expectations, strategy, plans, or intentions. Forward-looking statements contained in this Quarterly Report on Form 10-Q include, but are not limited to, statements about our future financial performance, our anticipated growth and growth strategies and our ability to effectively manage that growth, our ability to invest in and develop our products and services to operate with changing technology, our anticipated expansion and growth in Gross Payment Volume (GPV) and revenue, our plans for international expansion, the expected closing and impact of our recent proposed acquisitions, our plans with respect to patents and other intellectual property, our expectations regarding litigation, our expectations regarding share-based compensation, our expectations regarding the impacts of accounting guidance, our expectations regarding restricted cash, and the sufficiency of our cash and cash equivalents and cash generated from operations to meet our working capital and capital expenditure requirements.

The outcome of the events described in these forward-looking statements is subject to known and unknown risks, uncertainties, and other factors described in the section titled “Risk Factors” and elsewhere in this Quarterly Report on Form 10-Q.

All forward-looking statements are based on information and estimates available to the Company at the time of this Quarterly Report on Form 10-Q and are not guarantees of future performance. We undertake no obligation to update any forward-looking statements made in this Quarterly Report on Form 10-Q to reflect events or circumstances after the date of this Quarterly Report on Form 10-Q or to reflect new information or the occurrence of unanticipated events, except as required by law.

Part I—Financial Information
Item 1. Financial Statements
SQUARE, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)
(In thousands, except share and per share data)

	March 31, 2018	December 31, 2017
Assets		
Current assets:		
Cash and cash equivalents	$738,586	$696,474
Short-term investments	200,048	169,576
Restricted cash	27,688	28,805
Settlements receivable	700,646	620,523
Customer funds	152,661	103,042
Loans held for sale	78,821	73,420
Other current assets	91,933	86,454
Total current assets	1,990,383	1,778,294
Property and equipment, net	98,170	91,496
Goodwill	58,327	58,327
Acquired intangible assets, net	14,138	14,334
Long-term investments	176,672	203,667
Restricted cash	9,802	9,802
Other non-current assets	32,120	31,350
Total assets	$2,379,612	$2,187,270
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	$19,556	$16,763
Customers payable	881,754	733,736
Settlements payable	116,902	114,788
Accrued transaction losses	28,309	26,893
Accrued expenses	57,997	52,280
Other current liabilities	27,214	28,367
Total current liabilities	1,131,732	972,827
Long-term debt (Note 11)	362,965	358,572
Other non-current liabilities	74,935	69,538
Total liabilities	1,569,632	1,400,937
Commitments and contingencies (Note 16)		
Stockholders' equity:		
Preferred stock, $0.0000001 par value: 100,000,000 shares authorized at March 31, 2018 and December 31, 2017. None issued and outstanding at March 31, 2018 and December 31, 2017.	—	—
Class A common stock, $0.0000001 par value: 1,000,000,000 shares authorized at March 31, 2018 and December 31, 2017; 287,921,742 and 280,400,813 issued and outstanding at March 31, 2018 and December 31, 2017, respectively.	—	—
Class B common stock, $0.0000001 par value: 500,000,000 shares authorized at March 31, 2018 and December 31, 2017; 112,462,337 and 114,793,262 issued and outstanding at March 31, 2018 and December 31, 2017, respectively.	—	—
Additional paid-in capital	1,682,581	1,630,386
Accumulated other comprehensive loss	(1,294)	(1,318)

Accumulated deficit	(871,307)	(842,735)
Total stockholders’ equity	809,980	786,333
Total liabilities and stockholders’ equity	$2,379,612	$2,187,270

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

SQUARE, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)
(In thousands, except per share data)

	Three Months Ended March 31,	
	2018	2017
Revenue:		
Transaction-based revenue	$523,037	$403,478
Subscription and services-based revenue	97,054	49,060
Hardware revenue	14,417	9,016
Bitcoin revenue	34,095	—
Total net revenue	668,603	461,554
Cost of revenue:		
Transaction-based costs	327,911	257,778
Subscription and services-based costs	30,368	15,876
Hardware costs	19,702	12,662
Bitcoin costs	33,872	—
Amortization of acquired technology	1,580	1,807
Total cost of revenue	413,433	288,123
Gross profit	255,170	173,431
Operating expenses:		
Product development	105,095	68,582
Sales and marketing	77,266	49,900
General and administrative	75,501	56,935
Transaction, loan and advance losses	18,031	11,891
Amortization of acquired customer assets	269	205
Total operating expenses	276,162	187,513
Operating loss	(20,992)	(14,082)
Interest and other expense, net	2,819	499
Loss before income tax	(23,811)	(14,581)
Provision for income taxes	175	509
Net loss	$(23,986)	$(15,090)
Net loss per share:		
Basic	$(0.06)	$(0.04)
Diluted	$(0.06)	$(0.04)
Weighted-average shares used to compute net loss per share		
Basic	395,948	366,737
Diluted	395,948	366,737

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

SQUARE, INC.
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS
(Unaudited)
(In thousands)

	Three Months Ended March 31,	
	2018	2017
Net loss	$(23,986)	$(15,090)
Net foreign currency translation adjustments	549	757
Net unrealized gain (loss) on revaluation of intercompany loans	665	(29)
Net unrealized gain (loss) on marketable securities	(1,190)	19
Total comprehensive loss	$(23,962)	$(14,343)

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

SQUARE, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)
(In thousands)

	Three Months Ended March 31, 2018	2017
Cash flows from operating activities:		
Net loss	$(23,986)	$(15,090)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Depreciation and amortization	10,160	9,437
Non-cash interest and other expense	4,847	1,534
Share-based compensation	46,824	31,670
Transaction, loan and advance losses	18,031	11,891
Deferred provision (benefit) for income taxes	(654)	99
Changes in operating assets and liabilities:		
Settlements receivable	(81,452)	54,586
Customer funds	(49,619)	(13,953)
Purchase of loans held for sale	(344,976)	(252,170)
Sales and principal payments of loans held for sale	337,092	242,431
Other current assets	(13,444)	6,105
Other non-current assets	(1,256)	141
Accounts payable	1,990	(1,459)
Customers payable	147,977	(11,132)
Settlements payable	2,114	(15,378)
Charge-offs to accrued transaction losses	(12,842)	(11,178)
Accrued expenses	2,703	3,930
Other current liabilities	3,165	(368)
Other non-current liabilities	5,379	2,902
Net cash provided by operating activities	52,053	43,998
Cash flows from investing activities:		
Purchase of marketable securities	(50,221)	(181,851)
Proceeds from maturities of marketable securities	45,450	15,569
Proceeds from sale of marketable securities	—	3,996
Purchase of property and equipment	(8,083)	(6,508)
Purchase of intangible assets	(1,584)	—
Business acquisitions	(1,055)	(1,600)
Net cash used in investing activities	(15,493)	(170,394)
Cash flows from financing activities:		
Proceeds from issuance of convertible senior notes, net	—	428,250
Purchase of convertible senior note hedges	—	(92,136)
Proceeds from issuance of warrants	—	57,244
Payment for termination of Starbucks warrant	—	(54,808)
Principal payments on capital lease obligation	(665)	(247)
Proceeds from the exercise of stock options, net	31,354	39,280
Payments for tax withholding related to vesting of restricted stock units	(27,651)	—
Net cash provided by financing activities	3,038	377,583
Effect of foreign exchange rate on cash and cash equivalents	1,397	1,058
Net increase in cash, cash equivalents and restricted cash	40,995	252,245
Cash, cash equivalents and restricted cash, beginning of period	735,081	488,745

Cash, cash equivalents and restricted cash, end of period	$776,076	$740,990

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

SQUARE, INC.
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

NOTE 1 - DESCRIPTION OF BUSINESS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES
Business

Square, Inc. (together with its subsidiaries, Square or the Company) creates tools that help sellers start, run, and grow their businesses. Square enables sellers to accept card payments and also provides reporting and analytics, next-day settlement, and chargeback protection. Square’s point-of-sale software and other business services help sellers manage inventory, locations, and employees; access financing; engage customers; and grow sales. Cash App is an easy way for businesses and individuals to send and receive money, store their funds as well as use their funds via a Visa debit card, and recently started offering customers the ability to purchase bitcoin (a 'cryptocurrency' or 'digital currency'). Caviar is a food ordering service for pickup and delivery that helps restaurants reach new customers. Square was founded in 2009 and is headquartered in San Francisco, with offices in the United States, Canada, Japan, Australia, Ireland, and the United Kingdom.

Basis of Presentation

The accompanying interim condensed consolidated financial statements of the Company are unaudited. These interim condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States of America (U.S. GAAP) and the applicable rules and regulations of the Securities and Exchange Commission (SEC) for interim financial information. Accordingly, they do not include all of the information and footnotes required by U.S. GAAP for complete financial statements. The December 31, 2017 condensed consolidated balance sheet was derived from the audited financial statements as of that date, but does not include all of the information and footnotes required by U.S. GAAP for complete financial statements.

The accompanying unaudited interim condensed consolidated financial statements have been prepared on the same basis as the audited consolidated financial statements and, in the opinion of management, reflect all adjustments of a normal recurring nature considered necessary to state fairly the Company's consolidated financial position, results of operations, comprehensive loss, and cash flows for the interim periods. All intercompany transactions and balances have been eliminated in consolidation. The interim results for the three months ended March 31, 2018 are not necessarily indicative of the results that may be expected for the year ending December 31, 2018, or for any other future annual or interim period.

The information included in this Quarterly Report on Form 10-Q should be read in conjunction with “Management’s Discussion and Analysis of Financial Condition and Results of Operations,” “Quantitative and Qualitative Disclosures About Market Risk,” and the Consolidated Financial Statements and notes thereto included in Items 7, 7A, and 8, respectively, in the Company's Annual Report on Form 10-K for the year ended December 31, 2017.

Use of Estimates
The preparation of the Company’s consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue and expenses, as well as related disclosure of contingent assets and liabilities. Actual results could differ from the Company’s estimates. To the extent that there are material differences between these estimates and actual results, the Company’s financial condition or operating results will be materially affected. The Company bases its estimates on past experience and other assumptions that the Company believes are reasonable under the circumstances, and the Company evaluates these estimates on an ongoing basis.

Estimates, judgments, and assumptions in these consolidated financial statements include, but are not limited to, those related to revenue recognition, accrued transaction losses, valuation of the debt component of convertible senior notes, valuation of loans held for sale, goodwill and intangible assets, income and other taxes, and share-based compensation.

Concentration of Credit Risk

For the three months ended March 31, 2018 and 2017, the Company had no customer that accounted for greater than 10% of total net revenue.

The Company had three third-party payment processors that represented approximately 46%, 42%, and 7% of settlements receivable as of March 31, 2018. The same three parties represented approximately 46%, 42%, and 8% of settlements receivable as of December 31, 2017. All other third-party processors were insignificant.

Financial instruments that potentially subject the Company to concentrations of credit risk consist primarily of cash and cash equivalents, restricted cash, marketable securities, settlements receivables, customer funds, and loans held for sale. The associated risk of concentration for cash and cash equivalents and restricted cash is mitigated by banking with creditworthy institutions. At certain times, amounts on deposit exceed federal deposit insurance limits. The associated risk of concentration for marketable securities is mitigated by holding a diversified portfolio of highly rated investments. Settlements receivable are amounts due from well-established payment processing companies and normally take one or two business days to settle which mitigates the associated risk of concentration. The associated risk of concentration for loans held for sale is partially mitigated by credit evaluations that are performed prior to facilitating the offering of loans and ongoing performance monitoring of the Company’s loan customers.

Accounting Policies

Except for the adoption of ASC 606, Revenue from Contracts with Customers (ASC 606), described in Note 2, and the accounting policy on cryptocurrency transactions, described below, there have been no material changes to the Company’s accounting policies during the three months ended March 31, 2018, as compared to the accounting policies described in the Company’s Annual Report on Form 10-K for the year ended December 31, 2017.

Cryptocurrency transactions

During the fourth quarter of 2017, the Company started offering its Cash App customers the ability to purchase bitcoin, a cryptocurrency denominated asset, from the Company. The Company purchases bitcoin from public cryptocurrency exchanges or from customers. Upon purchase, the Company records the cost of bitcoin within other current assets in its consolidated balance sheets. Upon sale, the Company records the total sale amount received from customers as bitcoin revenue and the associated cost as cost of revenue. The carrying value of bitcoin was $0.2 million and $0.3 million as of March 31, 2018 and December 31, 2017, respectively. The Company assesses the carrying value of bitcoin at each reporting date and records an impairment charge if the cost exceeds the fair value. Losses on bitcoin for the three months ended March 31, 2018 were insignificant.

Recent Accounting Pronouncements

Recently issued accounting pronouncements not yet adopted

In February 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2016-02, Leases, which will require, among other items, lessees to recognize a right of use asset and a related lease liability for most leases on the balance sheet. Qualitative and quantitative disclosures will be enhanced to better understand the amount, timing and uncertainty of cash flows arising from leases. This guidance is effective for financial statements issued for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years, with early adoption permitted. The new standard should be applied on a modified retrospective basis. The Company does not plan to early adopt this guidance. The Company’s operating leases primarily comprise of office spaces, with the most significant leases relating to corporate headquarters in San Francisco and an office in New York. While the Company continues to evaluate the impact of adopting this guidance on its consolidated financial statements, it does expect to record right to use assets and related lease liabilities on its consolidated balance sheets upon adoption, which will increase total assets and liabilities.

In June 2016, the FASB issued ASU No. 2016-13, Measurement of Credit Losses on Financial Instruments, which requires measurement and recognition of expected credit losses for financial assets held. This guidance is effective for financial statements issued for fiscal years beginning after December 15, 2019, and interim periods within those fiscal years, with early adoption permitted. The Company is currently evaluating the impact this new guidance may have on the consolidated financial statements and related disclosures.

In January 2017, the FASB issued ASU No. 2017-04, Simplifying the Test for Goodwill Impairment. The new guidance eliminates the requirement to calculate the implied fair value of goodwill assuming a hypothetical purchase price allocation (i.e., Step 2 of the goodwill impairment test) to measure a goodwill impairment charge. Instead, entities will record an impairment charge based on the excess of a reporting unit's carrying amount over its fair value, not to exceed the carrying amount of goodwill. This standard should be adopted when the Company performs its annual or any interim goodwill impairment tests in fiscal years beginning after December 15, 2019, with early adoption permitted. The amendments should be applied on a prospective basis. The Company does not expect the adoption of this guidance to have a material the impact on the consolidated financial statements and related disclosures.

In March 2017, the FASB issued ASU No. 2017-08, Premium Amortization on Purchased Callable Debt Securities, which amends the amortization period for certain purchased callable debt securities held at a premium, shortening such period to the earliest call date. This standard is effective for annual periods beginning after December 15, 2018, and interim periods within those fiscal years, with early adoption permitted. The amendments in this guidance should be applied on a modified retrospective basis through a cumulative-effect adjustment directly to retained earnings as of the beginning of the period of adoption. The Company is currently evaluating the impact this new guidance may have on the consolidated financial statements and related disclosures.

In February 2018, the FASB issued ASU 2018-02, Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income. When the Tax Cuts and Jobs Act of 2017 was enacted in December 2017, there was a valuation allowance on the deferred tax assets included within the Company's accumulated other comprehensive income; therefore no tax expense resulted from the change in the federal income tax rate. This guidance allows companies to reclassify such tax effects from accumulated other comprehensive income to retained earnings. This guidance is effective for financial statements issued for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years, with early adoption permitted. The Company does not expect the adoption of this guidance to have a material impact on the consolidated financial statements and related disclosures.

In February 2018, the FASB issued ASU 2018-03, Recognition and Measurement of Financial Assets and Financial Liabilities. This guidance clarifies that an entity that uses the measurement alternative for equity securities without readily determinable fair values can change its measurement approach to fair value. This guidance is effective for financial statements issued for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years beginning after June 15, 2018. The Company does not expect the adoption of this guidance to have a material impact on the consolidated financial statements and related disclosures.
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NOTE 2 - REVENUE

Adoption of ASC 606, Revenue from Contracts with Customers

On January 1, 2018, the Company adopted ASC 606 using the modified retrospective method applied to those contracts which were not completed as of January 1, 2018. Results for reporting periods beginning after January 1, 2018 are presented under ASC 606, while prior period amounts are not adjusted and continue to be reported in accordance with the Company's historic revenue recognition methodology under ASC 605, Revenue Recognition.

The Company recorded a net reduction to retained earnings of $4.6 million as of January 1, 2018, due to the cumulative impact of adopting ASC 606, primarily related to impact on revenue and associated cost of revenue from hardware sold through the retail distribution channels and hardware installment sales. The impact to revenue for the three months ended March 31, 2018, was an increase of $1.3 million as a result of applying ASC 606.

For the three months ended March 31, 2018, the revenue recognized from contracts with customers was $648.8 million, including $34.1 million from bitcoin sales. Revenue from other sources was $19.8 million. Impairment losses arising from contracts with customers were not significant in the current reporting period.

The impact of adoption of ASC 606 on the Company's consolidated statement of operations and balance sheet was as follows (in thousands):

	Three Months Ended March 31, 2018		
	As reported	Balances without adoption of ASC 606	Effect of change
Impact on the Condensed Consolidated Statement of Operations:			
Subscription and services-based revenue	$97,054	$96,995	$59
Hardware revenue	14,417	13,154	1,263
Subscription and services-based costs	30,368	30,368	—
Hardware costs	19,702	18,757	945
Impact on the Condensed Consolidated Balance Sheets:			
Other current assets	91,933	100,573	(8,640)
Other current liabilities	27,214	31,976	(4,762)
Other non-current assets	32,120	33,355	(1,235)
Other non-current liabilities	$74,935	$75,993	$(1,058)

Revenue Recognition

Revenue is recognized when control of the promised goods or services is transferred to our customers, in an amount that reflects the consideration the Company expects to be entitled to in exchange for those goods or services. The Company's contracts with customers generally do not include multiple performance obligations.

The following table presents the Company's revenue from contracts with customers disaggregated by revenue source (in thousands):

	Three Months Ended March 31,	
	2018	2017
Revenue from Contracts with Customers:		
Transaction-based revenue	$523,037	$403,478
Subscription and services-based revenue	77,215	31,321
Hardware revenue	$14,417	$9,016
Bitcoin revenue	$34,095	$—

Transaction-based revenue

The Company charges its sellers a transaction fee for managed payments solutions that is generally calculated as a percentage of the total transaction amount processed. The Company selectively offers custom pricing for certain sellers. The Company collects the transaction amount from the seller's customer's bank, net of acquiring interchange and assessment fees, processing fees and bank settlement fees paid to third-party payment processors and financial institutions. The Company retains its fees and remits the net amount to the sellers.

The Company acts as the merchant of record for its sellers and works directly with payment card networks and banks so that its sellers do not need to manage the complex systems, rules, and requirements of the payments industry. The Company satisfies its performance obligations and therefore recognizes the transaction fees as revenue upon authorization of a transaction by the seller's customer's bank.

Revenue is recognized net of refunds, which arise from reversals of transactions initiated by sellers.

The transaction fees collected from sellers are recognized as revenue on a gross basis as the Company is the principal in the delivery of the managed payments solutions to the sellers. The Company has concluded it is the principal because it controls the services before delivery to the seller, it is primarily responsible for the delivery of the services and it has discretion in setting prices charged to sellers. As the merchant of record, Square is liable for settlement of the transactions the Company processes for its sellers, which is recorded as cost of revenues.

Subscription and services-based revenue

Subscription and services-based revenue is primarily comprised of revenue the Company generates from Instant Deposit, Caviar and various software as a service (SaaS) products.

Instant Deposit is a functionality within the Cash App and the Company's managed payment solutions that enables customers, including individuals and sellers, to instantly deposit funds into their bank accounts. The Company charges a per transaction fee which is recognized as revenue when customers instantly deposit funds to their bank account.

Caviar is a food ordering platform that facilitates food delivery services for restaurants. The Company's performance obligation is the delivery of food orders from restaurants to customers. The Company charges fees to restaurants, as sellers, and also charges delivery and service fees to customers. All fees are billed upon delivery of food orders, when the Company considers that it has satisfied its performance obligations. Revenue is also recognized upon delivery of the food orders, net of refunds. Refunds are estimated based on historical experience.

SaaS represents software products and solutions that provide customers with access to various technologies for a fee which is recognized ratably as the service is provided. The Company's contracts with customers are generally for a term of one month and renew automatically each month. The Company invoices its customers monthly. The Company considers that it satisfies its performance obligations over time each month as it provides the SaaS services to customers and hence recognizes revenue ratably over the month.

Hardware revenue

The Company generates revenue through the sale of hardware through e-commerce and through its retail distribution channels. The Company satisfies its performance obligation upon delivery of hardware to its customers who include end user customers, distributors, or retailers. The Company may at times offer concessions to customers and also allows for customer returns, which are accounted for as variable consideration. The Company estimates these amounts based on historical experience, and reduces revenue recognized. The Company invoices end user customers upon delivery of the products to customers and payments from such customers are due upon invoicing. Distributors and retailers have payment terms that range from 30 to 90 days after delivery.

The Company offers hardware installment sales to customers with terms ranging from three to twenty four months. The Company allocates a portion of the consideration received from these arrangements to a financing component when it determines that a significant financing component exists. The financing component is subsequently recognized as financing revenue over the terms of the arrangement with the customer.

Bitcoin revenue

During the fourth quarter of 2017, the Company started offering its Cash App customers the ability to purchase bitcoin, a cryptocurrency denominated asset, from the Company. The Company satisfies its performance obligation and records revenue when bitcoin is transferred to the customer's account.

Arrangements with Multiple Performance Obligations

Infrequently the Company has offered its hardware customers free managed payment solutions with the purchase of its hardware as part of a marketing promotion. For such arrangements, the Company allocates revenue to each performance obligation based on its relative standalone selling price. We generally determine standalone selling prices based on the prices charged to customers since the Company's products and services are normally sold on a stand alone basis.

Deferred revenues

Deferred revenue is comprised of unearned revenue related to managed payments services offered in conjunction with hardware sales for which the cash payments from customers are received and due upon the sale of the hardware.

The deferred revenue balances were as follows (in thousands):

	Three Months Ended March 31,	
	2018	2017
Deferred revenue, beginning of the period	$5,893	$5,407
Deferred revenue, end of the period	3,353	2,965
Revenue recognized in the period from amounts included in deferred revenue at the beginning of the period	298	4,062

Practical Expedients

The Company does not recognize a financing component for hardware installment sales that have a term of one year or less.

NOTE 3 - RESTRICTED CASH

As of March 31, 2018 and December 31, 2017, restricted cash of $27.7 million and $28.8 million, respectively, is related to pledged cash deposited into savings accounts at the financial institutions that process the Company's sellers' payment transactions and as collateral pursuant to an agreement with the originating bank for the Company's loan product. The Company uses the restricted cash to secure letters of credit with the financial institution to provide collateral for cash flow timing differences in the processing of these payments. The Company has recorded this amount as a current asset on the consolidated balance sheets due to the short-term nature of these cash flow timing differences and that there is no minimum time frame during which the cash must remain restricted. Additionally, this balance includes certain amounts held as collateral pursuant to multi-year lease agreements, discussed in the paragraph below, which we expect to become unrestricted within the next year.

As of both March 31, 2018 and December 31, 2017, the remaining restricted cash of $9.8 million, is primarily related to cash deposited into money market funds that is used as collateral pursuant to multi-year lease agreements entered into in 2012 and 2014 (Note 16). The Company has recorded this amount as a non-current asset on the consolidated balance sheets as the terms of the related leases extend beyond one year.

NOTE 4 - FAIR VALUE OF FINANCIAL INSTRUMENTS

The Company measures its cash equivalents and short-term and long-term investments at fair value. The Company classifies its cash equivalents and short-term and long-term investments within Level 1 or Level 2 of the fair value hierarchy because the Company values these investments using quoted market prices or alternative pricing sources and models utilizing market observable inputs.
The Company’s financial assets and liabilities that are measured at fair value on a recurring basis are classified as follows (in thousands):

	March 31, 2018			December 31, 2017		
	Level 1	Level 2	Level 3	Level 1	Level 2	Level 3
Cash and Cash Equivalents:						
Money market funds	$405,813	$—	$ —	$387,698	$—	$ —
Commercial paper	—	20,576	—	—	24,695	—
Short-term securities:						
U.S. agency securities	—	13,583	—	—	15,083	—
Corporate bonds	—	91,672	—	—	57,798	—
Commercial paper	—	14,286	—	—	17,428	—
Municipal securities	—	26,889	—	—	23,700	—
U.S. government securities	53,618		—	55,567	—	—
Long-term securities:						
U.S. agency securities	—	20,095	—	—	20,169	—
Corporate bonds	—	71,383	—	—	91,413	—
Municipal securities	—	14,519	—	—	26,224	—
U.S. government securities	70,675	—	—	65,861	—	—
Total	$530,106	$273,003	$ —	$509,126	$276,510	$ —

The carrying amounts of certain financial instruments, including cash equivalents, settlements receivable, customer funds, accounts payable, customers payable, and settlements payable, approximate their fair values due to their short-term nature.

The Company estimates the fair value of its convertible senior notes based on their last actively traded prices (Level 1) or market observable inputs (Level 2). The estimated fair value and carrying value of the convertible senior notes were as follows (in thousands):

	March 31, 2018		December 31, 2017	
	Carrying Value	Fair Value (Level 2)	Carrying Value	Fair Value (Level 2)
Convertible senior notes	$362,965	$963,965	$358,572	$719,356
Total	$362,965	$963,965	$358,572	$719,356

Loans held for sale are recorded at the lower of amortized cost or fair value determined on an individual loan basis. To determine the fair value the Company utilizes industry-standard valuation modeling, such as discounted cash flow models, taking into account the estimated timing and amounts of periodic repayments.

A summary of loans disclosed at fair value on a recurring basis is as follows (in thousands):

	March 31, 2018		December 31, 2017	
	Carrying Value	Fair Value (Level 3)	Carrying Value	Fair Value (Level 3)
Loans held for sale	$78,821	$81,459	$73,420	$76,070
Total	$78,821	$81,459	$73,420	$76,070

The Company recognizes a charge within transaction, loan and advance losses on the consolidated statement of operations whenever the amortized cost of a loan exceeds its fair value, with such charges being reversed for subsequent increases in fair value, but only to the extent that such reversals do not result in the amortized cost of a loan exceeding its fair value. For the three months ended March 31, 2018, the Company recorded a charge for the excess of amortized cost over fair value of the loans of $2.5 million. No charges were recorded for the three months ended March 31, 2017.

If applicable, the Company will recognize transfers into and out of levels within the fair value hierarchy at the end of the reporting period in which the actual event or change in circumstance occurs. During the three months ended March 31, 2018 and 2017, the Company did not have any transfers in or out of Level 1, Level 2, or Level 3 assets or liabilities.

NOTE 5 - INVESTMENTS

The Company determines the appropriate classification of its investments in marketable securities at the time of purchase and reevaluates such designation at each balance sheet date. The Company has classified and accounted for its marketable securities as available-for-sale.

The Company's short-term and long-term investments as of March 31, 2018 are as follows (in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Short-term securities:				
U.S. agency securities	$13,581	$ 5	$ (3)	$13,583
Corporate bonds	92,023	11	(362)	91,672
Commercial paper	14,286	—	—	14,286
Municipal securities	26,950	20	(81)	26,889
U.S. government securities	53,615	11	(8)	53,618
Total	$200,455	$ 47	$ (454)	$200,048
Long-term securities:				
U.S. agency securities	$20,169	$ 8	$ (82)	$20,095
Corporate bonds	71,741	170	(528)	71,383
Municipal securities	14,467	70	(18)	14,519
U.S. government securities	71,078	—	(403)	70,675

Total	$ 177,455	$ 248	$ (1,031)	$ 176,672

The Company's short-term and long-term investments as of December 31, 2017 are as follows (in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Short-term securities:				
U.S. agency securities	$ 15,122	$ —	$ (39)	$ 15,083
Corporate bonds	57,855	22	(79)	57,798
Commercial paper	17,428	—	—	17,428
Municipal securities	23,743	8	(51)	23,700
U.S. government securities	55,729	1	(163)	55,567
Total	$ 169,877	$ 31	$ (332)	$ 169,576
Long-term securities:				
U.S. agency securities	$ 20,288	$ 2	$ (121)	$ 20,169
Corporate bonds	91,959	25	(571)	91,413
Municipal securities	26,371	13	(160)	26,224
U.S. government securities	66,362	19	(520)	65,861
Total	$ 204,980	$ 59	$ (1,372)	$ 203,667

For the periods presented, gains or losses realized on the sale of investments were not material. Investments are reviewed periodically to identify possible other-than-temporary impairments. As the Company has the ability and intent to hold these investments with unrealized losses until a recovery of fair value, or for a reasonable period of time sufficient for the recovery of fair value, which may be maturity, the Company does not consider these investments to be other-than-temporarily impaired for any of the periods presented.

The contractual maturities of the Company's short-term and long-term investments as of March 31, 2018 are as follows (in thousands):

	Amortized Cost	Fair Value
Due in one year or less	$ 200,455	$ 200,048
Due in one to five years	177,455	176,672
Total	$ 377,910	$ 376,720

NOTE 6 - PROPERTY AND EQUIPMENT, NET

The following is a summary of property and equipment, less accumulated depreciation and amortization (in thousands):

	March 31, 2018	December 31, 2017
Leasehold improvements	$ 82,425	$ 77,073
Computer equipment	70,818	66,186
Capitalized software	39,268	35,063
Office furniture and equipment	15,152	14,490
	207,663	192,812
Less: Accumulated depreciation and amortization	(109,493)	(101,316)
Property and equipment, net	$ 98,170	$ 91,496

Depreciation and amortization expense on property and equipment was $8.3 million for the three months ended March 31, 2018. Depreciation and amortization expense on property and equipment was $7.3 million for the three months ended March 31, 2017.

NOTE 7 - GOODWILL

Goodwill is recorded when the consideration paid for an acquisition of a business exceeds the fair value of identifiable net tangible and intangible assets acquired. As of both March 31, 2018 and December 31, 2017, goodwill was $58.3 million.

The Company performs a goodwill impairment test annually on December 31 and more frequently if events and circumstances indicate that the asset might be impaired. For the periods presented, the Company had recorded no impairment charges.

NOTE 8 - ACQUIRED INTANGIBLE ASSETS

For the three months ended March 31, 2018, the Company did not make any material acquisitions.

The following table presents the detail of acquired intangible assets as of the periods presented (in thousands):

	Balance at March 31, 2018		
	Cost	Accumulated Amortization	Net
Patents	$1,285	$ (585)	$700
Technology Assets	30,837	(22,909)	7,928
Customer Assets	10,319	(4,809)	5,510
Total	$42,441	$ (28,303)	$14,138

	Balance at December 31, 2017		
	Cost	Accumulated Amortization	Net
Patents	$1,285	$ (559)	$726
Technology Assets	29,158	(21,329)	7,829
Customer Assets	10,319	(4,540)	5,779
Total	$40,762	$ (26,428)	$14,334

The weighted average amortization periods for acquired patents, acquired technology, and customer intangible assets are approximately 13 years, 4 years, and 9 years, respectively.

Amortization expense associated with other intangible assets was $1.9 million for the three months ended March 31, 2018. Amortization expense associated with other intangible assets was $2.1 million for the three months ended March 31, 2017.

The total estimated future amortization expense of these intangible assets as of March 31, 2018 is as follows (in thousands):

2018 (remaining 9 months)	$4,864
2019	4,002
2020	2,039
2021	892
2022	611
Thereafter	1,730
Total	$14,138

NOTE 9 - OTHER CONSOLIDATED BALANCE SHEET COMPONENTS (CURRENT)

Other Current Assets

The following table presents the detail of other current assets (in thousands):

	March 31, 2018	December 31, 2017
Inventory, net	$ 20,899	$ 16,777
Processing costs receivable	27,099	21,083
Prepaid expenses	14,743	14,473
Accounts receivable, net	9,876	8,606
Deferred hardware costs (i)	—	7,931
Deferred magstripe reader costs (ii)	2,677	2,469
Other	16,639	15,115
Total	$ 91,933	$ 86,454

(i) The deferred hardware costs represented costs associated with hardware sold through the retail distribution channels. The adoption of ASC 606 on January 1, 2018, has resulted in the recognition of such costs upon delivery of the hardware to the distribution channel.

(ii) The Company capitalizes the cost of its magstripe readers, including packaging and shipping costs, held on-hand by the Company as of each consolidated balance sheet date. Once the readers are shipped to a third-party distributor or an end-customer, they are recorded as marketing expense on the consolidated statements of operations.

Accrued Expenses

The following table presents the detail of accrued expenses (in thousands):

	March 31, 2018	December 31, 2017
Accrued payroll	$ 13,833	$ 9,103
Accrued professional fees	5,888	5,638
Accrued advertising and other marketing	7,279	6,723
Processing costs payable	10,166	10,145
Accrued non income tax liabilities	4,677	6,155
Accrued hardware costs	1,305	2,496
Other accrued liabilities	14,849	12,020
Total	$ 57,997	$ 52,280

Other Current Liabilities

The following table presents the detail of other current liabilities (in thousands):

	March 31, 2018	December 31, 2017
Square Capital payable (iii)	$ 6,450	$ 7,671
Square Payroll payable (iv)	2,865	2,850
Deferred revenue	3,353	5,893
Current portion of deferred rent	3,252	3,311
Accrued redemptions	1,110	1,036
Other	10,184	7,606
Total	$ 27,214	$ 28,367

(iii) Square Capital payable represents unpaid amounts arising from the purchase of loans or loan repayments collected on behalf of third parties.

(iv) Square Payroll payable represents amounts received from Square Payroll product customers that will be utilized to settle the customers employee payroll and related obligations.

NOTE 10 - OTHER CONSOLIDATED BALANCE SHEET COMPONENTS (NON-CURRENT)

Other Non-Current Assets

The following table presents the detail of other non-current assets (in thousands):

	March 31, 2018	December 31, 2017
Investment in privately held entity	$ 25,000	$ 25,000
Deposits	2,379	2,738
Debt issuance costs	719	788
Deferred tax assets	666	519
Other	3,356	2,305
Total	$ 32,120	$ 31,350

Other Non-Current Liabilities

The following table presents the detail of other non-current liabilities (in thousands):

	March 31, 2018	December 31, 2017
Statutory liabilities (i)	$ 44,468	$ 40,768
Deferred rent	22,241	20,349
Deferred tax liabilities	139	644
Other	8,087	7,777
Total	$ 74,935	$ 69,538

(i) Statutory liabilities represent loss contingencies that may arise from the Company's interpretation and application of certain guidelines and rules issued by various federal, state, local, and foreign regulatory authorities.

NOTE 11 - INDEBTEDNESS

Revolving Credit Facility

In November 2015, the Company entered into a revolving credit agreement with certain lenders, which extinguished the prior revolving credit agreement and provided for a $375.0 million revolving secured credit facility maturing in November 2020. This revolving credit agreement is secured by certain tangible and intangible assets.

Loans under the credit facility bear interest at the Company’s option of (i) a base rate based on the highest of the prime rate, the federal funds rate plus 0.50%, and an adjusted LIBOR rate for a one-month interest period, in each case plus a margin ranging from 0.00% to 1.00%, or (ii) an adjusted LIBOR rate plus a margin ranging from 1.00% to 2.00%. This margin is determined based on the Company’s total leverage ratio for the preceding four fiscal quarters. The Company is obligated to pay other customary fees for a credit facility of this size and type including an annual administrative agent fee of $0.1 million and an unused commitment fee of 0.15%. To date no funds have been drawn under the credit facility, with $375.0 million remaining available. The Company paid $0.1 million in unused commitment fees during both the three months ended March 31, 2018 and 2017. As of March 31, 2018, the Company was in compliance with all financial covenants associated with this credit facility.

Convertible Senior Notes

On March 6, 2017, the Company issued an aggregate principal amount of $400.0 million of convertible senior notes (Notes) and an additional 10% or $40.0 million pursuant to the exercise in full of the option to the initial purchasers to cover over-allotments. The Notes mature on March 1, 2022, unless earlier converted or repurchased, and bear interest at a rate of 0.375% payable semi-annually on March 1 and September 1 of each year. The Notes are convertible at an initial conversion rate of 43.5749 shares of the Company's Class A common stock per $1,000 principal amount of Notes, which is equivalent to an initial conversion price of approximately $22.95 per share of Class A common stock. Holders may convert their Notes at any time prior to the close of business on the business day immediately preceding December 1, 2021 only under the following circumstances: (1) during any calendar quarter (and only during such calendar quarter), if the last reported sale price of the Company's Class A common stock for at least 20 trading days (whether or not consecutive) during a period of 30 consecutive trading days ending on the last trading day of the immediately preceding calendar quarter is greater than or equal to 130% of the conversion price on each applicable trading day; (2) during the five business day period after any five consecutive trading day period (the measurement period) in which the trading price (as defined in the indenture governing the Notes) per $1,000 principal amount of Notes for each trading day of the measurement period was less than 98% of the product of the last reported sale price of the Company's Class A common stock and the conversion rate on each such trading day; or (3) upon the occurrence of specified corporate events, including certain distributions, the occurrence of a fundamental change (as defined in the indenture governing the Notes) or a transaction resulting in the Company's Class A common stock converting into other securities or property or assets. On or after December 1, 2021, up until the close of business on the second scheduled trading day immediately preceding the maturity date, a holder may convert all or any portion of its Notes regardless of the foregoing circumstances. Upon conversion, the Company will pay or deliver, as the case may be, cash, shares of its Class A common stock, or a combination of cash and shares of its Class A common stock, at the Company's election. It is the Company's current intent and policy to settle conversions through combination settlement with a specified dollar amount of $1,000 per $1,000 principal amount of Notes. The circumstances required to allow the holders to convert their Notes were met for the quarters commencing January 1, 2018 and April 1, 2018, respectively. As of May 1, 2018, no holders have converted or indicated their intention to convert their Notes.

In accounting for the issuance of the Notes, the Company separated the Notes into liability and equity components. The carrying amount of the liability component was calculated by measuring the fair value of a similar debt instrument that does not have an associated convertible feature. The carrying amount of the equity component representing the conversion option was $86.2 million and was determined by deducting the fair value of the liability component from the par value of the Notes. The equity component is not remeasured as long as it continues to meet the conditions for equity classification. The excess of the principal amount of the liability component over its carrying amount ("debt discount") is amortized to interest expense over the term of the Notes at an effective interest rate of 5.34% over the contractual terms of the Notes.

Debt issuance costs related to the Notes comprised of discounts and commissions payable to the initial purchasers of $11.0 million and third party offering costs of $0.8 million. The Company allocated the total amount incurred to the liability and equity components of the Notes based on their relative values. Issuance costs attributable to the liability component were $9.4 million and will be amortized to interest expense using the effective interest method over the contractual term. Issuance costs attributable to the equity component were netted with the equity component in stockholders' equity.

The Notes consisted of the following (in thousands):

	March 31, 2018	December 31, 2017
Principal	$440,000	$ 440,000
Less: unamortized debt discount	(69,425)	(73,384)
Less: unamortized debt issuance costs	(7,610)	(8,044)

Net carrying amount	$362,965	$ 358,572

The net carrying amount of the equity component of the Notes was as follows (in thousands):

	March 31, 2018	December 31, 2017
Debt discount related to value of conversion option	$86,203	$ 86,203
Less: allocated debt issuance costs	(2,302)	(2,302)
Equity component, net	$83,901	$ 83,901

The Company recognized interest expense on the Notes as follows (in thousands, except for percentages):

	Three Months Ended March 31,	
	2018	2017
Contractual interest expense based on 0.375% per annum	$413	$113
Amortization of debt discount and issuance costs	4,393	1,390
Total	$4,806	$1,503
Effective interest rate of the liability component	5.34 %	5.34 %

Convertible Note Hedge and Warrant Transactions

In connection with the offering of the Notes, the Company entered into convertible note hedge transactions with certain financial institutions (Counterparties) whereby the Company has the option to purchase a total of approximately 19.2 million shares of its Class A common stock at a price of approximately $22.95 per share. The total cost of the convertible note hedge transactions was $92.1 million. In addition, the Company sold warrants to the Counterparties whereby the Counterparties have the option to purchase a total of 19.2 million shares of the Company's Class A common stock at a price of approximately $31.18 per share. The Company received $57.2 million in cash proceeds from the sale of these warrants. Taken together, the purchase of the convertible note hedges and sale of the warrants are intended to reduce dilution from the conversion of the Notes and/or offset any cash payments the Company is required to make in excess of the principal amount of the converted Notes, as the case may be, and to effectively increase the overall conversion price from approximately $22.95 per share to approximately $31.18 per share. As these instruments are considered indexed to the Company's own stock and are considered equity classified, the convertible note hedges and warrants are recorded in stockholders' equity, are not accounted for as derivatives and are not remeasured each reporting period. The net costs incurred in connection with the convertible note hedge and warrant transactions were recorded as a reduction to additional paid-in capital on the condensed consolidated balance sheets.

NOTE 12 - ACCRUED TRANSACTION LOSSES

The Company is exposed to transaction losses due to chargebacks as a result of fraud or uncollectibility.
The following table summarizes the activities of the Company's reserve for transaction losses (in thousands):

	Three Months Ended March 31,	
	2018	2017
Accrued transaction losses, beginning of the period	$26,893	$20,064
Provision for transaction losses	14,258	11,558
Charge-offs to accrued transaction losses	(12,842)	(11,178)
Accrued transaction losses, end of the period	$28,309	$20,444

22

NOTE 13 - INCOME TAXES

The Company recorded an income tax expense of $0.2 million for the three months ended March 31, 2018, compared to income tax expense of $0.5 million for the three months ended March 31, 2017. The income tax expense recorded for the three months ended March 31, 2018 was primarily due to state and foreign income tax expense.

The Company's effective tax rate was (0.7)% for the three months ended March 31, 2018, compared to an effective tax rate of (3.5)% for the three months ended March 31, 2017. The difference between the effective tax rate and the federal statutory tax rate for the three months ended March 31, 2018 and March 31, 2017 primarily relates to the valuation allowance on the Company's deferred tax assets.

The Company's effective tax rate may be subject to fluctuation during the year as new information is obtained, which may affect the assumptions used to estimate the annual effective tax rate, including factors such as the mix of forecasted pre-tax earnings in the various jurisdictions in which the Company operates, valuation allowances against deferred tax assets, the recognition and de-recognition of tax benefits related to uncertain tax positions, and changes in or the interpretation of tax laws in jurisdictions where the Company conducts business.

As of March 31, 2018, the Company retains a full valuation allowance on its deferred tax assets in the U.S. and certain foreign jurisdictions. The realization of the Company's deferred tax assets depends primarily on its ability to generate taxable income in future periods. The amount of deferred tax assets considered realizable in future periods may change as management continues to reassess the underlying factors it uses in estimating future taxable income.

The tax provision for the three months ended March 31, 2018 and March 31, 2017, was calculated on a jurisdiction basis. The Company estimated the foreign income tax provision using the effective income tax rate expected to be applicable for the full year.

On December 22, 2017, the SEC issued Staff Accounting Bulletin No. 118 to address the application of U.S. GAAP in situations when a registrant does not have the necessary information available, prepared, or analyzed (including computations) in reasonable detail to complete the accounting for certain income tax effects of the Tax Cuts and Jobs Act of 2017. The accounting for all items is expected to be complete when the 2017 U.S. corporate income tax return is filed in 2018. Any differences between what was previously recorded and the final tax return amounts or estimates done for subsequent quarters are not expected to be material.

NOTE 14 - STOCKHOLDERS' EQUITY

The changes in total stockholders' equity were as follows (in thousands):

	Total stockholders' equity
Balance at December 31, 2017	$ 786,333
Net loss	(23,986)
Exercise of stock options	31,354
Vesting of early exercised stock options and other	136
Share-based compensation	48,356
Tax withholding related to vesting of restricted stock units	(27,651)
Cumulative adjustment for adoption of ASC 606	(4,586)
Change in other comprehensive loss	24
Balance at March 31, 2018	$ 809,980

Common Stock

The Company has authorized the issuance of Class A common stock and Class B common stock. Class A common stock and Class B common stock are referred to as "common stock" throughout these Notes to the Condensed Consolidated Financial Statements, unless otherwise noted. As of March 31, 2018, the Company was authorized to issue 1,000,000,000 shares of Class A common stock and 500,000,000 shares of Class B common stock, each with a par value of $0.0000001 per share. As of March 31, 2018, there were 287,921,742 shares of Class A common stock and 112,462,337 shares of Class B common stock outstanding. Options and awards granted following the Company's Initial Public Offering are related to underlying Class A common stock. Additionally, holders of Class B common stock are able to convert such shares into Class A common stock.

Stock Plans

The Company maintains two share-based employee compensation plans: the 2009 Stock Plan (2009 Plan) and the 2015 Equity Incentive Plan (2015 Plan). The 2015 Plan serves as the successor to the 2009 Plan. The 2015 Plan became effective as of November 17, 2015. Outstanding awards under the 2009 Plan continue to be subject to the terms and conditions of the 2009 Plan. Since November 17, 2015, no additional awards have been nor will be in the future granted under the 2009 Plan.

Under the 2015 Plan, shares of the Company's Class A common stock are reserved for the issuance of incentive and nonstatutory stock options, restricted stock awards, restricted stock units (RSUs), performance shares, and stock bonuses to qualified employees, directors, and consultants. The awards must be granted at a price per share not less than the fair market value at the date of grant. Initially, 30,000,000 shares were reserved under the 2015 Plan, and any shares subject to options or other similar awards granted under the 2009 Plan that expire, are forfeited, are repurchased by the Company, or otherwise terminate unexercised, will become available under the 2015 Plan. The number of shares available for issuance under the 2015 Plan will be increased on the first day of each fiscal year, in an amount equal to the least of (i) 40,000,000 shares, (ii) 5% of the outstanding shares on the last day of the immediately preceding fiscal year, or (iii) such number of shares determined by the Company’s board of directors or a committee thereof. As of March 31, 2018, the total number of shares subject to stock options and RSUs outstanding under the 2015 Plan was 24,960,627, and 65,895,253 shares were available for future issuance. As of March 31, 2018, the total number of shares subject to stock options and RSUs outstanding under the 2009 Plan was 38,069,996.

A summary of stock option activity for the three months ended March 31, 2018 is as follows (in thousands, except share and per share data):

	Number of Stock Options Outstanding	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value
Balance at December 31, 2017	47,270,091	$ 8.67	6.52	$1,229,103
Exercised	(4,213,775)	7.44		
Forfeited	(328,651)	12.04		
Balance at March 31, 2018	42,727,665	$ 8.76	6.33	$1,727,761
Options exercisable as of March 31, 2018	40,039,760	$ 8.47	6.20	$1,630,725

Restricted Stock Activity

Activity related to RSUs during the three months ended March 31, 2018 is set forth below:

	Number of RSUs	Weighted Average Grant Date Fair Value
Unvested as of December 31, 2017	21,317,525	$ 17.84
Granted	1,226,422	44.78
Vested	(1,625,534)	14.54
Forfeited	(615,455)	15.67
Unvested as of March 31, 2018	20,302,958	$ 19.80

Share-Based Compensation

The fair value of stock options and employee stock purchase plan rights are estimated on the date of grant using the Black-Scholes-Merton option valuation model. The fair value of RSUs is determined by the closing price of the Company's common stock on each grant date.

There were no stock options granted during the three months ended March 31, 2018 and 2017.

The following table summarizes the effects of share-based compensation on the Company's condensed consolidated statements of operations (in thousands):

	Three Months Ended March 31,	
	2018	2017
Cost of revenue	$31	$—
Product development	30,482	19,356
Sales and marketing	4,961	3,935
General and administrative	11,350	8,379
Total	$46,824	$31,670

The Company recorded $2.3 million of share-based compensation expense related to the Company's 2015 Employee Stock Purchase Plan during the three months ended March 31, 2018, compared to $1.9 million for the three months ended March 31, 2017, which are included in the table above.

The Company capitalized $1.5 million of share-based compensation expense related to capitalized software costs during the three months ended March 31, 2018, compared to $0.5 million for the three months ended March 31, 2017. As of March 31, 2018, there was $418.7 million of total unrecognized compensation cost related to outstanding stock options that is expected to be recognized over a weighted-average period of 2.74 years.

NOTE 15 - LOSS PER SHARE

Basic net loss per share is computed by dividing the net loss by the weighted-average number of shares of common stock outstanding during the period. Diluted loss per share is the same as basic loss per share for all periods presented because the effects of potentially dilutive items were anti-dilutive given the Company's net loss.

The following table presents the calculation of basic and diluted net loss per share (in thousands, except per share data):

	Three Months Ended March 31,	
	2018	2017
Net loss	$(23,986)	$(15,090)
Basic shares:		
Weighted-average common shares outstanding	397,246	368,571
Weighted-average unvested shares	(1,298)	(1,834)
Weighted-average shares used to compute basic net loss per share	395,948	366,737
Diluted shares:		
Weighted-average shares used to compute diluted loss per share	395,948	366,737
Net loss per share:		
Basic	$(0.06)	$(0.04)
Diluted	$(0.06)	$(0.04)

Additionally, since the Company expects to settle the principal amount of its outstanding Notes in cash, the Company uses the treasury stock method for calculating any potential dilutive effect of the conversion spread on diluted net income per share, if applicable. The conversion spread will have a dilutive impact on diluted net income per share of common stock when the average market price of the Company’s common stock for a given period exceeds the conversion price of $22.95 per share for the Notes. Because the Company has reported a net loss for all periods presented, diluted loss per share is the same as basic loss per share for those periods.

The following potential common shares were excluded from the calculation of diluted net loss per share because their effect would have been anti-dilutive for the periods presented (in thousands):

	Three Months Ended March 31,	
	2018	2017
Stock options and restricted stock units	66,382	84,909
Common stock warrants	19,173	11,129
Unvested shares	1,298	1,834
Employee stock purchase plan	264	509
Total anti-dilutive securities	87,117	98,381

NOTE 16 - COMMITMENTS AND CONTINGENCIES

Operating and Capital Leases

The Company has entered into various non-cancelable operating leases for certain offices with contractual lease periods expiring between 2018 and 2025. The Company recognized total rental expenses under operating leases of $4.5 million for the three months ended March 31, 2018, compared to $2.8 million for the three months ended March 31, 2017.

Future minimum lease payments under non-cancelable operating leases (with initial lease terms in excess of one year) and future minimum capital lease payments as of March 31, 2018 are as follows (in thousands):

	Capital	Operating
Year:		
2018 (remaining 9 months)	$1,996	$15,437
2019	2,549	19,600
2020	1,274	19,388
2021	44	19,009
2022	2	19,105
Thereafter	—	23,628
Total	$5,865	$116,167
Less amount representing interest	(15)	
Present value of capital lease obligations	5,850	
Less current portion of capital lease obligation	(2,654)	
Non-current portion of capital lease obligation	$3,196	

Litigation

The Company is currently a party to, and may in the future be involved in, various litigation matters (including intellectual property litigation), legal claims, and government investigations.

The Treasurer & Tax Collector of the City and County of San Francisco (Tax Collector) has issued a decision for fiscal years 2014 and 2015, that the Tax Collector believes the Company's primary business activity is financial services rather than information services, and accordingly the Company would be liable for the Gross Receipts Tax and Payroll Expense Tax under the rules for financial services business activities. The Company paid the liability for fiscal years 2014 and 2015 in the first quarter of 2018, as assessed by the Tax Collector. The Company intends to vigorously defend its position, which it believes has merit. Should the Company not prevail, the Company could be obligated to pay additional taxes together with any associated penalties and interest for subsequent years that together, in aggregate, could be material. The Company is currently unable to estimate the range of possible loss given the uncertainties associated with this matter, including uncertainties about the Tax Collector's rationale for its position and about the amounts that may ultimately be subject to such taxes.

In addition, from time to time, the Company is involved in various other litigation matters and disputes arising in the ordinary course of business. The Company cannot at this time fairly estimate a reasonable range of exposure, if any, of the potential liability with respect to these other matters. While the Company does not believe, at this time, that any ultimate liability resulting from any of these other matters will have a material adverse effect on the Company's results of operations, financial position, or liquidity, the Company cannot give any assurance regarding the ultimate outcome of these other matters, and their resolution could be material to the Company's operating results for any particular period.

NOTE 17 - SEGMENT AND GEOGRAPHICAL INFORMATION

Operating segments are defined as components of an enterprise for which discrete financial information is available that is evaluated regularly by the chief operating decision maker (CODM) for purposes of allocating resources and evaluating financial performance. The Company's CODM is the chief executive officer who reviews financial information presented on a consolidated basis for purposes of allocating resources and evaluating financial performance. As such, the Company's operations constitute a single operating segment and one reportable segment.

Revenue

Revenue by geography is based on the billing addresses of the merchants or customers. The following table sets forth revenue by geographic area (in thousands):

	Three Months Ended March 31,	
	2018	2017
Revenue		
United States	$640,173	$444,899
International	28,430	16,655
Total net revenue	$668,603	$461,554

No individual country from the international markets contributed in excess of 10% of total revenue for the three months ended March 31, 2018 and 2017.

Long-Lived Assets

The following table sets forth long-lived assets by geographic area (in thousands):

	March 31, 2018	December 31, 2017
Long-lived assets		
United States	$165,530	$ 158,820
International	5,105	5,337
Total long-lived assets	$170,635	$ 164,157

NOTE 18 - SUPPLEMENTAL CASH FLOW INFORMATION

The supplemental disclosures of cash flow information consist of the following (in thousands):

	Three Months Ended March 31,	
	2018	2017
Supplemental Cash Flow Data:		
Cash paid for interest	$966	$142
Cash paid for income taxes	658	334
Supplemental disclosures of non-cash investing and financing activities:		
Change in purchases of property and equipment in accounts payable and accrued expenses	(3,813)	(468)
Unpaid business acquisition purchase price	1,151	400

NOTE 19 - SUBSEQUENT EVENTS

Release of Caviar Shares Held Back

In 2014, in conjunction with the Company's acquisition of Caviar, Inc. (Caviar), 1,292,207 shares of the purchase consideration issuable were withheld for indemnification purposes. In April 2018, the Company reached an agreement with the former owners of Caviar whereby 822,085 of the shares held back would be released to the former owners and 469,894 shares would be forfeited back to the Company to cover any potential future liabilities.

28

Acquisition

In April 2018, the Company entered into an agreement to acquire Weebly Inc (Weebly), a technology company that provides customers with tools to build a professional website or online store, for a purchase price of approximately $265 million, comprising an aggregate of approximately $132.5 million in cash and approximately $132.5 million in the Company’s Class A common stock, subject to adjustments based on (i) purchase price adjustment provisions and (ii) indemnification obligations of Weebly stockholders after the closing of the acquisition, as specified in the agreement. The acquisition of Weebly will enable the Company to combine Weebly’s web presence tools with the Company's in-person and online offerings to create one cohesive solution for sellers to start or grow an omnichannel business. The acquisition will also expand the Company’s customer base globally and add a new recurring revenue stream. The acquisition is expected to close in the second quarter of 2018, subject to customary closing conditions including regulatory approvals.

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

You should read the following discussion and analysis in conjunction with the information set forth within the condensed consolidated financial statements and the notes thereto included elsewhere in this Quarterly Report on Form 10-Q. The statements in this discussion regarding our expectations of our future performance, liquidity and capital resources, our plans, estimates, beliefs and expectations that involve risks and uncertainties, and other non-historical statements in this discussion, are forward-looking statements. These forward-looking statements are subject to numerous risks and uncertainties, including, but not limited to, the risks and uncertainties described under “Risk Factors” and elsewhere in this Quarterly Report on Form 10-Q. Our actual results may differ materially from those contained in or implied by any forward-looking statements.

Overview

We started Square in February 2009 to enable businesses (sellers) to accept card payments, an important capability that was previously inaccessible to many businesses. However, sellers also need innovative solutions to thrive, and we have since expanded to provide additional products and services to give these businesses access to the same tools as large businesses. Square is a cohesive commerce ecosystem that helps our sellers start, run, and grow their businesses. We combine sophisticated software with affordable hardware to enable sellers to turn mobile and computing devices into powerful payment and point-of-sale solutions. We focus on technology and design to create products and services that are cohesive, fast, self-serve, and dependable.

The foundation of our ecosystem is a full service, managed payments offering. Once a seller downloads the Square Point of Sale mobile app, they can quickly and easily take their first payment, because we can typically bring them onto our system in minutes. With our offering, a seller can accept payments in person via magnetic stripe (a swipe), EMV (Europay, MasterCard, and Visa) (a dip), or NFC (Near Field Communication) (a tap); or online via Square Invoices, Square Virtual Terminal, or the seller’s website or app. Once on our system, sellers gain access to technology and features such as reporting and analytics, next-day settlements, digital receipts, payment dispute and chargeback management, security, and Payment Card Industry (PCI) compliance.

Our commerce ecosystem also includes powerful point-of-sale software and services that help sellers make informed business decisions through the use of analytics and reporting. As a result, sellers can manage orders, inventory, locations, employees, and payroll; engage and grow their sales with customers; and gain access to business loans through our Square Capital service. Some of these advanced point-of-sale features are broadly applicable to our seller base and include Employee Management and Customer Engagement. We have also extended our ecosystem to serve sellers with more specific needs. Our Build with Square developer platform (application programming interface or APIs) allows businesses with individualized needs to customize their business solutions while processing payments on

Square and taking advantage of all the services in our ecosystem, including integration with third-party applications. In addition, certain verticals, such as service and retail sellers, benefit from specific features such as Invoices, Appointments, and Square for Retail. We monetize these features through either a per transaction fee, a subscription fee, or a service fee.

In the same way that we have empowered businesses with fast, simple, and cohesive tools, we see an opportunity with our Cash App to build a similar ecosystem of services for individuals. The Cash App offers individuals access to a fast, easy way to send and receive money electronically to and from individuals and businesses. We also offer our Cash App customers the ability to store their funds as well as use their funds via a Visa debit card. We have recently added functionality to the Cash App to enable customers to buy bitcoin from us. Additionally, we give customers the option to sell bitcoin to us.

We also serve sellers through Caviar, our food ordering platform that helps restaurants reach new customers and increase sales without additional overhead. Caviar revenue consists of seller fees charged to restaurants, and delivery and service fees from consumers. All fees are recognized upon delivery of the food, net of refunds.

With Square Capital, we facilitate the offering of loans to sellers based on their payment processing history, and the product is broadly available across our seller base. We currently fund a majority of these loans from arrangements with institutional third-party investors who purchase these loans. We recognize revenue upon the sale of the loans to third-party investors or over time as the sellers pay down the outstanding amounts for the loans that we hold as available for sale. We also earn a servicing fee from third-party investors that we record as revenue as we provide the services.

We also provide hardware to facilitate commerce for sellers. This hardware includes magstripe readers, contactless and chip readers, chip card readers, Square Stand, Square Register and third-party peripherals.

We have grown rapidly to serve millions of sellers that represent a diverse set of industries, including retail, services, and food-related businesses, and sizes, ranging from a single vendor at a farmers' market to multi-location businesses. These sellers also span geographies including the United States, Canada, Japan, Australia, and the United Kingdom.

Results of Operations

Revenue (in thousands, except for percentages)

	Three Months Ended March 31,			
	2018	2017	$ Change	% Change
Transaction-based revenue	$523,037	$403,478	$119,559	30 %
Subscription and services-based revenue	97,054	49,060	47,994	98 %
Hardware revenue	14,417	9,016	5,401	60 %
Bitcoin revenue	$34,095	$—	$34,095	— %
Total net revenue	$668,603	$461,554	$207,049	45 %

Total net revenue for the three months ended March 31, 2018 increased by $207.0 million or 45%, compared to the three months ended March 31, 2017.

Transaction-based revenue for the three months ended March 31, 2018 increased by $119.6 million or 30%, compared to the three months ended March 31, 2017. This increase was attributable to growth in Gross Payment Volume (GPV) processed for the three months ended March 31, 2018 of 31%, compared to the three months ended March 31, 2017. We continue to benefit from growth in processed volumes from our existing sellers, in addition to meaningful contributions from new sellers. Additionally, GPV from larger sellers, which we define as all sellers that generate more than $125,000 in annualized GPV, represented 47% of our GPV in the first quarter of 2018, an increase from 43% in the first quarter of 2017. We continue to see ongoing success with attracting and enabling large seller growth, which will help us to drive strong GPV growth as we scale.

Subscription and services-based revenue for the three months ended March 31, 2018 increased by $48.0 million or 98%, compared to the three months ended March 31, 2017. The increases were primarily driven by continued growth of Instant Deposit, Caviar, and Square Capital, which were also the largest contributors to subscription and services-based revenue. Subscription and services-based revenue contributed 15% of total net revenue in the three months ended March 31, 2018, compared to 11% in the three months ended March 31, 2017.

Hardware revenue for the three months ended March 31, 2018 increased by $5.4 million or 60%, compared to the three months ended March 31, 2017. The increase primarily reflects growth in shipments of Square Register following its launch in the fourth quarter of 2017. Square Register is our first all-in-one offering that combines our hardware, point-of-sale software, and payments technology. The increase was also driven by continued growth in sales of our Square Stand and third-party peripherals driven primarily by new features and product offerings. Additionally, the adoption of ASC 606 resulted in an increase of $1.3 million in hardware revenue primarily related to the earlier revenue recognition of hardware sold through the retail distribution channels and hardware installment sales, which were previously recorded upon sell through to the end user customer.

During the fourth quarter of 2017, we started offering our Cash App customers the ability to purchase bitcoin from us. Bitcoin revenue comprises total sale amount we receive from bitcoin sales to customers and is recorded upon transfer of bitcoin to the customer's account. The sale amount generally includes a small margin added to the price we pay to purchase bitcoin and accordingly, the amount of bitcoin revenue will fluctuate depending on the volatility of market bitcoin prices and customer demand.

Total Cost of Revenue (in thousands, except for percentages)

	Three Months Ended March 31,			
	2018	2017	$ Change	% Change
Transaction-based costs	$327,911	$257,778	$70,133	27 %
Subscription and services-based costs	30,368	15,876	14,492	91 %
Hardware costs	19,702	12,662	7,040	56 %
Bitcoin costs	33,872	—	33,872	— %
Amortization of acquired technology	1,580	1,807	(227)	(13)%
Total cost of revenue	$413,433	$288,123	$125,310	43 %

Total cost of revenue for the three months ended March 31, 2018 increased by $125.3 million or 43%, compared to the three months ended March 31, 2017.

Transaction-based costs for the three months ended March 31, 2018 increased by $70.1 million or 27%, compared to the three months ended March 31, 2017. This increase was attributable to growth in GPV processed for the three months ended March 31, 2018 of 31%, compared to the three months ended March 31, 2017. Additionally, transaction-based margin as a percentage of GPV was 1.09% for the three months ended March 31, 2018, up from 1.07% for the three months ended March 31, 2017. Transaction-based profit continued to benefit from higher margin products and improvements in our transaction cost profile. GPV from higher margin products such as Invoices, Virtual Terminal, and eCommerce API payments more than doubled year over year.

Subscription and services-based costs for the three months ended March 31, 2018 increased by $14.5 million or 91%, compared to the three months ended March 31, 2017, primarily reflecting increased costs associated with the growth of Caviar and, to a lesser extent, increased costs associated with the growth of Instant Deposit.

Hardware costs for the three months ended March 31, 2018 increased by $7.0 million or 56%, compared to the three months ended March 31, 2017. The increase in hardware costs reflects growth in our sales of Square Register, Square Stand and third-party peripherals as described above. Additionally, the adoption of ASC 606 resulted in an increase of $0.9 million in hardware costs primarily related to earlier recognition of costs of hardware sold through the retail distribution channels and hardware installment sales in line with the revenue recognition for such sales under ASC 606.

Bitcoin costs comprises of the amounts we pay to purchase bitcoin in the public cryptocurrency exchanges or from customers. The amount of bitcoin costs will fluctuate in line with the associated revenue.

Amortization of acquired technology assets for the three months ended March 31, 2018 decreased by $0.2 million or 13%, compared to the three months ended March 31, 2017, as a result of certain technology assets reaching end of life.

31

Operating Expenses (in thousands, except for percentages)

	Three Months Ended March 31,			
	2018	2017	$ Change	% Change
Product development	$105,095	$68,582	$36,513	53 %
% of total net revenue	16 %	15 %		
Sales and marketing	$77,266	$49,900	$27,366	55 %
% of total net revenue	12 %	11 %		
General and administrative	$75,501	$56,935	$18,566	33 %
% of total net revenue	11 %	12 %		
Transaction, loan and advance losses	$18,031	$11,891	$6,140	52 %
% of total net revenue	3 %	3 %		
Amortization of acquired customer assets	$269	$205	$64	31 %
% of total net revenue	— %	— %		
Total operating expenses	$276,162	$187,513	$88,649	47 %

Product development expenses for the three months ended March 31, 2018 increased by $36.5 million or 53%, compared to the three months ended March 31, 2017, primarily due to an increase of $30.2 million in personnel-related costs mainly in our engineering, product, data science and design teams. The increase in personnel-related costs includes an increase in share-based compensation expense of $11.1 million.

Sales and marketing expenses for the three months ended March 31, 2018 increased by $27.4 million or 55%, compared to the three months ended March 31, 2017, primarily due to the following:

- an increase of $12.3 million in costs associated with our Cash App peer-to-peer transfer service as result of continued growth of this product. Of this increase, $3.0 million relates to losses due to chargebacks from peer-to-peer transfer service;
- an increase of $6.8 million in advertising costs primarily from increased online and mobile marketing campaigns during the period; and
- an increase of $5.6 million in sales and marketing personnel costs to enable growth initiatives. The increase in personnel- related costs includes an increase in share-based compensation expense of $1.0 million.

General and administrative expenses for the three months ended March 31, 2018 increased by $18.6 million or 33%, compared to the three months ended March 31, 2017, primarily due to the following:

- an increase of $13.7 million in general and administrative personnel costs, mainly as a result of additions to our finance, legal, and customer success personnel as we continue to add resources and skills as our business scales to support long-term growth. The increase in personnel-related costs includes an increase in share-based compensation expense of $3.0 million; and

- an increase of $1.9 million in various tax and licensing expenses as we continue to expand our business and product offerings.

Transaction, loan and advance losses for the three months ended March 31, 2018 increased by $6.1 million or 52%, compared to the three months ended March 31, 2017, primarily due to the following:

- a $2.5 million charge recorded to loan losses in the three months ended March 31, 2018, with no similar charges during the prior year, as a result of the growth and increasing maturity of our Square Capital loan portfolio, and continued refinement of inputs to our loan loss estimation methodology. We record loan losses when the amortized cost of a loan exceeds the estimated fair value of the loan, as determined at the individual loan level; and

-

growth in GPV. Transaction losses increased to a lesser extent than GPV growth due to ongoing investment in data science and improvements in our risk operations to mitigate exposure to transaction losses.

Amortization of acquired customer assets for the three months ended March 31, 2018 increased by $0.1 million or 31%, compared to the three months ended March 31, 2017, as a result of certain customer assets reaching end of life offset by additional customer assets acquired.

Interest and Other Expense, Net (in thousands, except for percentages)

	Three Months Ended March 31,			
	2018	2017	$ Change	% Change
Interest and other expense, net	$2,819	$499	$ 2,320	465 %

Interest and other expense, net, for the three months ended March 31, 2018 increased by $2.3 million, compared to the three months ended March 31, 2017, primarily due to interest expense related to our convertible notes issued in March 2017, offset in part by income earned on our investment in marketable securities and foreign exchange rate gains.

Provision for Income Taxes (in thousands, except for percentages)

	Three Months Ended March 31,			
	2018	2017	$ Change	% Change
Provision for income taxes	$175	$509	$ (334)	(66)%
Effective tax rate	(0.7)%	(3.5)%		

Provision for income taxes for the three months ended March 31, 2018 decreased by $0.3 million, compared to the three months ended March 31, 2017, due to a change in the mix of U.S. and international income offset by a release in the U.S. valuation allowance.

Key Operating Metrics and Non-GAAP Financial Measures

We collect and analyze operating and financial data to evaluate the health of our business, allocate our resources, and assess our performance. In addition to total net revenue, net income (loss), and other results under generally accepted accounting principles (GAAP), the following table sets forth key operating metrics and non-GAAP financial measures we use to evaluate our business. We believe these metrics and measures are useful to facilitate period-to-period comparisons of our business, and to facilitate comparisons of our performance to that of other payments solution providers.

	Three Months Ended March 31,	
	2018	2017
	(in thousands, except GPV)	
Gross Payment Volume (GPV) (in millions)	$17,827	$13,647
Adjusted Revenue	$306,820	$203,776
Adjusted EBITDA	$35,894	$27,025
Adjusted Net Income Per Share:		
Basic	$0.07	$0.05
Diluted	$0.06	$0.05

Gross Payment Volume (GPV)

We define GPV as the total dollar amount of all card payments processed by sellers using Square, net of refunds. Additionally, GPV includes Cash App activity related to peer-to-peer payments sent from a credit card and Cash for

Business.

Adjusted Revenue

Adjusted Revenue is a non-GAAP financial measure that we define as our total net revenue less transaction-based costs and bitcoin costs. We believe it is useful to subtract transaction-based costs and bitcoin costs from total net revenue to derive Adjusted Revenue as this is a primary metric used by management to measure our business performance, and it affords greater comparability to other payments solution providers. Substantially all of the transaction-based costs are interchange and assessment fees, processing fees and bank settlement fees paid to third-party payment processors and financial institutions. While some payments solution providers present their revenue in a similar fashion to us, others present their revenue net of transaction-based costs because, unlike us, they pass through these costs directly to their sellers and are not deemed the principal in these arrangements. Under our standard pricing model, we do not pass through these costs directly to our sellers. We also deduct bitcoin costs because we consider our role in the bitcoin transactions to be facilitating customer access to bitcoin. Since we only apply a small margin to the market cost of bitcoin when we sell bitcoin to customers, and we have no control over the cost of bitcoin in the market which tends to be volatile, we believe deducting bitcoin costs is a better reflection of the economic benefits as well as the Company's performance from the bitcoin transactions.

Adjusted Revenue has limitations as a financial measure, should be considered as supplemental in nature, and is not meant as a substitute for the related financial information prepared in accordance with GAAP. These limitations include the following:

- Adjusted Revenue is net of transaction-based costs, which is our largest cost of revenue item;
- Adjusted Revenue is net of bitcoin costs, which could be a significant cost; and
- other companies, including companies in our industry, may calculate Adjusted Revenue differently or not at all, which reduces its usefulness as a comparative measure.

Because of these limitations, you should consider Adjusted Revenue alongside other financial performance measures, including total net revenue and our financial results presented in accordance with GAAP. The following table presents a reconciliation of total net revenue to Adjusted Revenue for each of the periods indicated:

	Three Months Ended March 31,	
	2018	2017
	(in thousands)	
Total net revenue	$668,603	$461,554
Less: transaction-based costs	327,911	257,778
Less: bitcoin costs	33,872	—
Adjusted Revenue	$306,820	$203,776

Adjusted EBITDA, Adjusted Net Income (Loss), and Adjusted Net Income (Loss) Per Share

Adjusted EBITDA, Adjusted Net Income (Loss), and Adjusted Net Income (Loss) Per Share are non-GAAP financial measures that represent our net income (loss) and net income (loss) per share, adjusted to eliminate the effect of certain items as described below. We have included these non-GAAP financial measures in this Quarterly Report on Form 10-Q because they are key measures used by our management to evaluate our operating performance, generate future operating plans, and make strategic decisions, including those relating to operating expenses and the allocation of internal resources. Accordingly, we believe these measures provide useful information to investors and others in understanding and evaluating our operating results in the same manner as our management and board of directors. In addition, they provide useful measures for period-to-period comparisons of our business, as they remove the effect of certain non-cash items and certain variable charges.

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We believe it is useful to exclude non-cash charges, such as amortization of intangible assets, and share-based compensation expenses, from our non-GAAP financial measures because the amount of such expenses in any specific period may not directly correlate to the underlying performance of our business operations.

- In connection with the issuance of our convertible senior notes (as described in Note 11), we are required to recognize non-cash interest expense related to amortization of debt discount and issuance costs. We believe that excluding these expenses from our non-GAAP measures is useful to investors because such incremental non-cash interest expense does not represent a current or future cash outflow for the Company and is therefore not indicative of our continuing operations or meaningful when comparing current results to past results.

- We exclude the gain or loss on the sale of property and equipment, and impairment of intangible assets, as applicable, from non-GAAP financial measures because we do not believe that these items are reflective of our ongoing business operations.

In addition to the items above, Adjusted EBITDA as a non-GAAP financial measure also excludes depreciation, other cash interest income and expense, other income and expense and provision or benefit from income taxes, as these items are not components of our core business operations.

Non-GAAP financial measures have limitations, should be considered as supplemental in nature and are not meant as a substitute for the related financial information prepared in accordance with GAAP. These limitations include the following:

- share-based compensation expense has been, and will continue to be for the foreseeable future, a significant recurring expense in our business and an important part of our compensation strategy;

- the intangible assets being amortized may have to be replaced in the future, and the non-GAAP financial measures do not reflect cash capital expenditure requirements for such replacements or for new capital expenditures or other capital commitments; and

- non-GAAP measures do not reflect changes in, or cash requirements for, our working capital needs.

In addition to the limitations above, Adjusted EBITDA as a non-GAAP financial measure does not reflect the effect of depreciation expense and related cash capital requirements, income taxes that may represent a reduction in cash available to us, and the effect of foreign currency exchange gains or losses which is included in other income and expense.

Other companies, including companies in our industry, may calculate the non-GAAP financial measures differently or not at all, which reduces their usefulness as comparative measures.

Because of these limitations, you should consider the non-GAAP financial measures alongside other financial performance measures, including net loss and our other financial results presented in accordance with GAAP.

The following table presents a reconciliation of net loss to Adjusted EBITDA for each of the periods indicated (in thousands):

	Three Months Ended March 31,	
	2018	2017
	(in thousands)	
Net loss	$(23,986)	$(15,090)
Share-based compensation expense	46,824	31,670
Depreciation and amortization	10,160	9,437
Interest and other expense, net	2,819	499
Provision for income taxes	175	509
Gain on sale of property and equipment	(98)	—
Adjusted EBITDA	$35,894	$27,025

35

The following table presents a reconciliation of net loss to Adjusted Net Income (Loss) and Adjusted Net Income (Loss) Per Share for each of the periods indicated (in thousands, except per share data):

	Three Months Ended March 31,	
	2018	2017
	(in thousands)	
Net loss	$(23,986)	$(15,090)
Share-based compensation expense	46,824	31,670
Amortization of intangible assets	1,851	2,121
Amortization of debt discount and issuance costs	4,393	1,390
Gain on sale of property and equipment	(98)	—
Adjusted Net Income	$28,984	$20,091
Adjusted Net Income Per Share:		
Basic	$0.07	$0.05
Diluted	$0.06	$0.05
Weighted-average shares used to compute Adjusted Net Income Per Share:		
Basic	395,948	366,737
Diluted	461,761	404,319

Basic Adjusted Net Income (Loss) Per Share is computed by dividing the Adjusted Net Income (Loss) by the weighted-average number of shares of common stock outstanding during the period.

Diluted Adjusted Net Income Per Share is computed by dividing Adjusted Net Income by the weighted-average number of shares of common stock outstanding adjusted for the dilutive effect of all potential shares of common stock.

Liquidity and Capital Resources

The following table summarizes our cash, cash equivalents, restricted cash, and investments in marketable securities (in thousands):

	March 31, 2018	December 31, 2017
Cash and cash equivalents	$738,586	$ 696,474
Short-term restricted cash	27,688	28,805
Long-term restricted cash	9,802	9,802
Cash, cash equivalents, and restricted cash	$776,076	$ 735,081
Short-term investments	200,048	169,576
Long-term investments	176,672	203,667
Cash, cash equivalents, restricted cash and investments in marketable securities	$1,152,796	$ 1,108,324

The following table summarizes our cash flow activities (in thousands):

	Three Months Ended March 31,	
	2018	2017
Net cash provided by operating activities	$52,053	$43,998
Net cash used in investing activities	(15,493)	(170,394)
Net cash provided by financing activities	3,038	377,583
Effect of foreign exchange rate on cash and cash equivalents	1,397	1,058
Net increase in cash, cash equivalents and restricted cash	$40,995	$252,245

Our principal sources of liquidity are our cash and cash equivalents and investments in marketable securities. As of March 31, 2018, we had $1,115.3 million of cash and cash equivalents and investments in marketable securities, which were held primarily in cash deposits, money market funds, U.S. government and agency securities, commercial paper, and corporate bonds. We consider all highly liquid investments with an original maturity of three months or less when purchased to be cash equivalents. Our investments in marketable securities are classified as available-for-sale.

On March 6, 2017, we issued $440.0 million in aggregate principal amount of convertible senior notes (Notes) that mature on March 1, 2022, unless earlier converted or repurchased, and bear interest at a rate of 0.375% payable semi-annually on March 1 and September 1 of each year. The Notes are convertible at an initial conversion rate of 43.5749 shares of Class A common stock per $1,000 principal amount of Notes, which is equivalent to an initial conversion price of approximately $22.95 per share of Class A common stock. In connection with the offering of the Notes, we entered into convertible note hedge transactions with certain financial institutions (Counterparties) whereby we have the option to purchase a total of approximately 19.2 million shares of our Class A common stock at a price of approximately $22.95 per share. The total cost of the convertible note hedge transactions was approximately $92.1 million. In addition, we sold warrants to the Counterparties whereby the Counterparties have the option to purchase a total of approximately 19.2 million shares of our Class A common stock at a price of approximately $31.18 per share. We received approximately $57.2 million in cash proceeds from the sale of these warrants. Taken together, the purchase of the convertible note hedges and sale of the warrants are intended to offset any actual dilution from the conversion of the Notes. The net proceeds from this transaction, after issuance costs was approximately $393.4 million. See Note 11, Indebtedness, of the Notes to the Condensed Consolidated Financial Statements for more details on these transactions.

In addition, we have a revolving secured credit facility that matures in November 2020. To date, no funds have been drawn under the credit facility, with $375.0 million remaining available. Loans under the credit facility bear interest at our option of (i) a base rate based on the highest of the prime rate, the federal funds rate plus 0.50%, and an adjusted LIBOR rate for a one-month interest period, in each case plus a margin ranging from 0.00% to 1.00%, or (ii) an adjusted LIBOR rate plus a margin ranging from 1.00% to 2.00%. This margin is determined based on our total leverage ratio for the preceding four fiscal quarters. We are obligated to pay other customary fees for a credit facility of this size and type including an annual administrative agent fee of $0.1 million and an unused commitment fee of 0.15%.

We believe that our existing cash and cash equivalents, marketable securities, and availability under our line of credit will be sufficient to meet our working capital needs, including any expenditures related to strategic transactions and investment commitments that we may from time to time enter into, and planned capital expenditures for at least the next 12 months. From time to time, we may seek to raise additional capital through equity, equity-linked, and debt financing arrangements. We cannot provide assurance that any additional financing will be available to us on acceptable terms or at all.

Short-term restricted cash of $27.7 million as of March 31, 2018 reflects pledged cash deposited into savings accounts at the financial institutions that process our sellers' payments transactions and as collateral pursuant to an agreement with the originating bank for the Company's loan product. We use the restricted cash to secure letters of credit with these financial institutions to provide collateral for liabilities arising from cash flow timing differences in the processing of these payments. We have recorded this amount as a current asset on our consolidated balance sheets given the short-term nature of these cash flow timing differences and that there is no minimum time frame during which the cash must remain restricted. Additionally, this balance includes certain amounts held as collateral pursuant to multi-year lease agreements, discussed in the paragraph below, which we expect to become unrestricted within the next year.

Long-term restricted cash of $9.8 million as of March 31, 2018 reflects cash deposited into money market accounts that is used as collateral pursuant to multi-year lease agreements entered into in 2012 and 2014 for our office buildings. The Company has recorded this amount as a non-current asset on the consolidated balance sheets as the lease terms extend beyond one year.

We experience significant day-to-day fluctuations in our cash and cash equivalents due to fluctuations in settlements receivable and customers payable, and hence working capital. These fluctuations are primarily due to:

- Timing of period end. For periods that end on a weekend or a bank holiday, our cash and cash equivalents, settlements receivable, and customers payable amounts typically will be more than for periods ending on a weekday, as we settle to our sellers for payment processing activity on business days; and
- Fluctuations in daily GPV. When daily GPV increases, our cash and cash equivalents, settlements receivable, and customers payable amounts increase. Typically our settlements receivable and customers payable balances at period end represent one to four days of receivables and disbursements to be made in the subsequent period. Customers payable and settlements receivable balances typically move in tandem, as pay-out and pay-in largely occur on the same business day. However, customers payable balances will be greater in amount than settlements receivable balances due to the fact that a subset of funds are held due to unlinked bank accounts, risk holds, and chargebacks. Holidays and day-of-week may also cause significant volatility in daily GPV amounts.

Cash Flows from Operating Activities

Cash provided by operating activities consisted of net loss adjusted for certain non-cash items including depreciation and amortization, non-cash interest and other expense, share-based compensation expense, transaction, loan and advance losses, deferred income taxes, and the cumulative adjustment for adoption of ASC 606, as well as the effect of changes in operating assets and liabilities, including working capital.

For the three months ended March 31, 2018, cash provided by operating activities was $52.1 million, primarily as a result of:

- Net loss of $24.0 million, offset by non-cash items consisting primarily of share-based compensation of $46.8 million, transaction, loan and advance losses of $18.0 million, and depreciation and amortization of $10.2 million. These items are largely driven by growth and expansion of our business activities.

- Additional cash provided from changes in operating assets and liabilities, including increases in customers payable of $148.0 million. Customers payable balances increased significantly compared to as of December 31, 2017 primarily due to the increase in GPV at the end of the period. These balances are largely offset by settlements receivable, described below, which moves in tandem.

- Offset in part by cash used from changes in operating assets and liabilities, including increases in settlements receivable of $81.5 million for reasons aforementioned, increases in customer funds of $49.6 million as result of an increasing customer base with stored funds on the Cash App, and charge-offs to accrued transaction losses of $12.8 million arising as a result of growth in GPV.

For the three months ended March 31, 2017, cash provided by operating activities was $44.0 million, primarily as a result of:

- Net loss of $15.1 million, offset by non-cash items consisting primarily of share-based compensation of $31.7 million, provision for transaction losses of $11.9 million, and depreciation and amortization of $9.4 million.
- Additional cash provided from changes in operating assets and liabilities, including decreases in settlements receivable of $54.6 million.
- Offset in part by cash used from changes in operating assets and liabilities, including decreases in customers payable of $11.1 million, decreases in settlements payable of $15.4 million, increases in customer funds of $14.0 million and

charge-offs and recoveries to accrued transaction losses of $11.2 million.

Cash Flows from Investing Activities

Cash flows used in investing activities primarily relate to capital expenditures to support our growth, investments in marketable securities, and business acquisitions.

For the three months ended March 31, 2018, cash used in investing activities was $15.5 million, primarily as a result of the purchase of marketable securities of $50.2 million, offset in part by proceeds from maturities of marketable securities of $45.5 million. Additional uses of cash were as a result of the purchase of property and equipment of $8.1 million.

For the three months ended March 31, 2017, cash used in investing activities was $170.4 million primarily as a result of the purchase of marketable securities of $181.9 million, offset in part by proceeds from maturities and sales of marketable securities of $19.6 million. Additional uses of cash were as a result of the purchase of property and equipment of $6.5 million.

Cash Flows from Financing Activities

For the three months ended March 31, 2018, cash provided by financing activities was $3.0 million as a result of proceeds from issuances of common stock from the exercise of options of $31.4 million, offset in part by payments for employee tax withholding related to vesting of restricted stock units of $27.7 million.

For the three months ended March 31, 2017, cash provided by financing activities was $377.6 million as a result of $393.4 million in net proceeds from the Notes offering and as a result of proceeds from issuances of common stock from the exercise of options of $39.3 million, offset in part by the settlement of the warrant with Starbucks of $54.8 million.

Contractual Obligations and Commitments

There were no material changes in our commitments under contractual obligations, except for scheduled payments from the ongoing business, as disclosed in our Annual Report on Form 10-K for the year ended December 31, 2017.

Off-Balance Sheet Arrangements

We do not have any off-balance sheet arrangements during the periods presented.

Critical Accounting Policies and Estimates

Our discussion and analysis of our financial condition and results of operations are based upon our financial statements, which have been prepared in accordance with GAAP. GAAP requires us to make certain estimates and judgments that affect the amounts reported in our financial statements. We base our estimates on historical experience, anticipated future trends, and other assumptions we believe to be reasonable under the circumstances. Because these accounting policies require significant judgment, our actual results may differ materially from our estimates.

We believe accounting policies and the assumptions and estimates associated with accrued transaction losses and revenue recognition have the greatest potential effect on our consolidated financial statements. Therefore, we consider these to be our critical accounting policies and estimates.

Our critical accounting policies are disclosed in our Annual Report on Form 10-K for the year ended December 31, 2017. Except for the adoption of ASC 606, Revenue from Contracts with Customers, as discussed further in Note 2 of the Notes to the Condensed Consolidated Financial Statements, our critical accounting policies have not materially changed during the three months ended March 31, 2018.

Revenue Recognition

Application of the various accounting principles in U.S. GAAP requires that we make judgments and estimates related to the classification, measurement and recognition of revenue. Complex arrangements may require significant judgment in contract interpretation to determine the appropriate accounting. Specifically, under ASC 606, the determination of whether we are a principal in the delivery of managed payments solutions and sale of bitcoin, and therefore recognize the revenue on a gross basis, or we are an agent and therefore recognize revenue on a net basis can require considerable judgment. We have concluded that we are the principal in these arrangements because we control the services or product before delivery to the customers.

Recent Accounting Pronouncements

See “Recent Accounting Pronouncements” described in Note 1 of the Notes to the Condensed Consolidated Financial Statements.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

We have operations both within the United States and globally, and we are exposed to market risks in the ordinary course of our business, including the effects of interest rate changes and foreign currency fluctuations. Information relating to quantitative and qualitative disclosures about these market risks is described below.

Interest Rate Sensitivity

Our cash and cash equivalents, and marketable securities as of March 31, 2018, were held primarily in cash deposits, money market funds, U.S. government and agency securities, commercial paper, and corporate bonds. The fair value of our cash, cash equivalents, and marketable securities would not be significantly affected by either an increase or decrease in interest rates due mainly to the short-term nature of a majority of these instruments. Additionally, we have the ability to hold these instruments until maturity if necessary to reduce our risk. Any future borrowings incurred under our credit facility would accrue interest at a floating rate based on a formula tied to certain market rates at the time of incurrence (as described above). A hypothetical 100 basis point increase or decrease in interest rates would not have a material effect on our financial results.

Foreign Currency Risk

Most of our revenue is earned in U.S. dollars, and therefore our revenue is not currently subject to significant foreign currency risk. Our foreign operations are denominated in the currencies of the countries in which our operations are located, and may be subject to fluctuations due to changes in foreign currency exchange rates, particularly changes in the Japanese Yen, Canadian Dollar, Australian Dollar, Euro and British Pound. Fluctuations in foreign currency exchange rates may cause us to recognize transaction gains and losses in our statement of operations. A 10% increase or decrease in current exchange rates would not have a material impact on our financial results.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our Chief Executive Officer and our Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures as of the end of the period covered by this Quarterly Report on Form 10-Q. The term “disclosure controls and procedures,” as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the “Exchange Act”), means controls and other procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC’s rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company’s management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure. Management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives and management necessarily applies its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Based on such evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that, as of such date, our disclosure controls and procedures were effective at the reasonable assurance level.

Changes in Internal Control over Financial Reporting

On January 1, 2018, we adopted ASC 606, Revenue from Contracts with Customers. As a result of the adoption, changes were made to our processes related to revenue recognition and the control activities within them, in order to monitor and maintain appropriate controls over financial reporting. There were no other changes in our internal control over financial reporting identified in connection with the evaluation required by Rules 13a-15(d) and 15d-15(d) of the Exchange Act that occurred during the period covered by this Quarterly Report on Form 10-Q that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Part II—Other Information

Item 1. Legal Proceedings

We are currently a party to, and may in the future be involved in, various litigation matters (including intellectual property litigation), legal claims, and government investigations.

We were involved in a class action lawsuit concerning independent contractors in connection with our Caviar business. On March 19, 2015, Jeffry Levin, on behalf of a putative nationwide class, filed a lawsuit in the United States District Court for the Northern District of California against our wholly owned subsidiary, Caviar, Inc., which, as amended, alleged that Caviar misclassified Mr. Levin and other similarly situated couriers as independent contractors and, in doing so, violated various provisions of the California Labor Code and California Business and Professions Code by requiring them to pay various business expenses that should have been borne by Caviar. The Court compelled arbitration of Mr. Levin's individual claims on November 16, 2015 and dismissed the lawsuit in its entirety with prejudice on May 2, 2016. On June 1, 2016, Mr. Levin filed a Notice of Appeal of the Court's order compelling arbitration with the United States Court of Appeals for the Ninth Circuit. Mr. Levin filed his opening appellate brief regarding the order compelling arbitration of his individual claims on October 7, 2016. We filed our answering brief on December 7, 2016, and Mr. Levin filed his reply on December 21, 2016. No hearing date was set. Mr. Levin also sought an award of penalties pursuant to the Labor Code Private Attorneys General Act of 2004 (PAGA). The parties stipulated that Mr. Levin would no longer pursue this PAGA claim but that it may instead be pursued by a different courier. Subsequently, couriers Nadezhda Rosen and La'Dell Brewster filed a new PAGA-only claim in the Superior Court of the State of California for the County of San Francisco (Superior Court) on November 7, 2016. Plaintiffs claimed that Caviar misclassified its couriers as independent contractors resulting in numerous violations of the California Labor Code, pursuant to which plaintiffs sought statutory penalties for those violations. In February 2017, we participated in a mediation with the parties in these Caviar misclassification suits to explore resolution of the matters at hand. After continued negotiation, the parties reached a global settlement of these suits, which has been confirmed. As a result, the Levin and Rosen lawsuits were dismissed with prejudice in their respective courts on January 24, 2018 and January 18, 2018, respectively.

In addition, from time to time, we are involved in various other litigation matters and disputes arising in the ordinary course of business. We cannot at this time fairly estimate a reasonable range of exposure, if any, of the potential liability with respect to these other matters. While we do not believe, at this time, that any ultimate liability resulting from any of these other matters will have a material adverse effect on our results of operations, financial position, or liquidity, we cannot give any assurance regarding the ultimate outcome of these other matters, and their resolution could be material to our operating results for any particular period.

Item 1A. Risk Factors

Investing in our securities involves a high degree of risk. You should carefully consider the risks and uncertainties described below, together with all of the other information in this Quarterly Report on Form 10-Q, including the section titled "Management's Discussion and Analysis of Financial Condition and Results of Operations" and our condensed consolidated financial statements and related notes, before making any investment decision with respect to our securities. The risks and uncertainties described below may not be the only ones we face. If any of the risks actually occur, our business could be materially and adversely affected. In that event, the market price of our Class A common stock could decline, and you could lose part or all of your investment.

The following description of risk factors includes any material changes to, and supersedes the description of, risk factors associated with the Company's business previously disclosed in Part I, Item 1A of our Annual Report on Form 10-K for the fiscal year ended December 31, 2017 under the heading "Risk Factors."

Risks Related to Our Business and Our Industry

Our business depends on a strong and trusted brand, and any failure to maintain, protect, and enhance our brand would hurt our business.

We have developed a strong and trusted brand that has contributed significantly to the success of our business. Our brand is predicated on the idea that our customers will trust us and find value in building and growing their businesses with our products and services. We believe that maintaining and promoting our brand in a cost-effective manner is critical to achieving widespread acceptance of our products and services and expanding our base of customers. Maintaining and promoting our brand will depend largely on our ability to continue to provide useful, reliable, secure and innovative products and services, as well as our ability to maintain trust and be a technology leader. We may introduce, or make changes to, features, products, services, or terms of service that customers do not like, which may materially and adversely affect our brand. Our brand promotion activities may not generate customer awareness or increase revenue, and even if they do, any increase in revenue may not offset the expenses we incur in building our brand. If we fail to successfully promote and maintain our brand or if we incur excessive expenses in this effort, our business could be materially and adversely affected.

The introduction and promotion of new services, as well as the promotion of existing services, may be partly dependent on our visibility on third-party advertising platforms, such as Google, Twitter, or Facebook. Changes in the way these platforms operate or changes in their advertising prices or other terms could make the maintenance and promotion of our products and services and our brand more expensive or more difficult. If we are unable to market and promote our brand on third-party platforms effectively, our ability to acquire new customers would be materially harmed. We also use retail partners to sell hardware and acquire customers. Our ability to acquire new customers could be materially harmed if we are unable to enter into or maintain these partnerships on terms that are commercially reasonable to us, or at all.

Harm to our brand can arise from many sources, including failure by us or our partners and service providers to satisfy expectations of service and quality; inadequate protection of sensitive information; compliance failures and claims; litigation and other claims; employee misconduct; and misconduct by our partners, service providers, or other counterparties. We have also received a significant amount of media coverage since our formation. We have also been from time to time in the past, and may in the future be, the target of incomplete, inaccurate, and misleading or false statements about our company, our business, and our products and services that could damage our brand and deter people and enterprises from adopting our services. Any negative publicity about our industry or our company, the quality and reliability of our products and services, our risk management processes, changes to our products and services, our ability to effectively manage and resolve customer complaints, our privacy, data protection, and information security practices, litigation, regulatory activity, and the experience of our customers with our products or services, could adversely affect our reputation and the confidence in and use of our products and services. If we do not successfully maintain a strong and trusted brand, our business could be materially and adversely affected.

As our revenue has increased, our growth rate has slowed at times in the past, and may decline in the future. Future revenue growth depends on our ability to retain existing sellers, attract new sellers, and increase sales to both new and existing sellers.

Our total net revenue grew from $1,267.1 million in 2015 to $1,708.7 million in 2016 and to $2,214.3 million in 2017. During the three months ended March 31, 2017 and 2018, our total net revenue grew from $461.6 million to $668.6 million, respectively. Our rate of revenue has slowed at times in the past, and may decline in the future, and it may decline more quickly than we expect for a variety of reasons, including the risks described in this Quarterly Report on Form 10-Q. Our customers have no obligation to continue to use our services, and we cannot assure you that they will. We generally do not have long-term contracts with our sellers, and the difficulty and costs associated with switching to a competitor may not be significant for many of our services. Our sellers' payment processing activity with us may decrease for a variety of reasons, including sellers' level of satisfaction with our products and services, the effectiveness of our support services, our pricing, the pricing and quality of competing products or services, the effects of global economic conditions, or reductions in our sellers' customer spending levels. In addition, the growth of our business depends in part on existing sellers expanding their use of our products and services. If we are unable to encourage sellers to broaden their use of our services, our growth may slow or stop, and our business may be materially and adversely affected. The growth of our business also depends on our ability to attract new sellers, to encourage larger sellers to use our products and services, and to introduce successful new products and services. We have invested and will continue to invest in improving our Square platform in order to offer better or new features, products and services, but if those features, products and services fail to be successful, our growth may slow or decline.

Our business has generated net losses, and we intend to continue to invest substantially in our business. Thus, we may not be able to achieve or maintain profitability.

We generated net losses of $62.8 million, $171.6 million, and $212.0 million for the years ended December 31, 2017, 2016 and 2015, respectively. During the three months ended March 31, 2018 and 2017, we generated net losses of $24.0 million and $15.1 million, respectively.

As of March 31, 2018, we had an accumulated deficit of $871.3 million. We intend to continue to make significant investments in our business, including with respect to our employee base; sales and marketing, including expenses relating to increased direct marketing efforts, referral programs, and free hardware and subsidized services; development of new products, services, and features; acquisitions; expansion of office space and other infrastructure; expansion of international operations; and general administration, including legal, finance, and other compliance expenses related to being a public company. If the costs associated with acquiring and supporting new or larger sellers materially rise in the future, including the fees we pay to third parties to advertise our products and services, our expenses may rise significantly. In addition, increases in our seller base could cause us to incur increased losses because costs associated with new sellers are generally incurred up front, while revenue is recognized thereafter as sellers utilize our services. If we are unable to generate adequate revenue growth and manage our expenses, we may continue to incur significant losses and may not achieve or maintain profitability.

From time to time, we may make decisions that will have a negative effect on our short-term operating results if we believe those decisions will improve the experiences of our customers, which we believe will improve our operating results over the long term. These decisions may not be consistent with the expectations of investors and may not produce the long-term benefits that we expect, in which case our business may be materially and adversely affected.

We, our sellers, our partners, and others who use our services obtain and process a large amount of sensitive data. Any real or perceived improper or unauthorized use of, disclosure of, or access to such data could harm our reputation as a trusted brand, as well as have a material and adverse effect on our business.

We, our sellers, and our partners, including third-party data centers that we use, obtain and process large amounts of sensitive data, including data related to our sellers, their customers, and their transactions, as well as other users of our services, such as Cash App and Square Payroll. We face risks, including to our reputation as a trusted brand, in the handling and protection of this data, and these risks will increase as our business continues to expand to include new products and technologies. Our operations involve the storage and transmission of sensitive information of individuals using our services, including their names, addresses, social security numbers (or their foreign equivalents), payment card numbers and expiration dates, bank account information, and data regarding the performance of our sellers' businesses. We also obtain sensitive information regarding our sellers' customers, including their contact information, payment card numbers and expiration dates, and purchase histories. Additionally, certain of our products and services are subject to the Health Insurance Portability and Accountability Act of 1996 (and the rules and regulations thereunder, as amended, including with respect to the HITECH Act) (HIPAA), and therefore we are required to take measures to safeguard protected health information of our sellers and their customers. Our services also provide third party developers the opportunity to provide applications to our sellers in our app marketplace. Sellers who choose to use such applications can grant permission allowing the applications to access content created or held by sellers in their Square account.

We have administrative, technical, and physical security measures in place, and we have policies and procedures in place to contractually require third parties to whom we transfer data to implement and maintain appropriate privacy and security measures. However, if our privacy and security measures or those of the previously mentioned third parties are inadequate or are breached as a result of third-party action, employee error, malfeasance, malware, phishing, hacking attacks, system error, trickery, or otherwise, and, as a result, someone obtains unauthorized access to funds, cryptocurrencies, including bitcoin, or sensitive information, including personally identifiable information or protected health information, on our systems or our partners' systems, or if we suffer a ransomware or advanced persistent threat attack, or if any of the foregoing is reported or perceived to have occurred, our reputation and business could be damaged. If the sensitive information is lost or improperly disclosed or threatened to be disclosed, we could incur significant liability and be subject to regulatory scrutiny and penalties, including costs associated with remediation.

Under payment card rules and our contracts with our card processors, if there is a breach of payment card information that we store or that is stored by our sellers or other third parties with which we do business, we could be liable to the payment card issuing banks for their cost of issuing new cards and other related expenses. Additionally, if our own confidential business information were improperly disclosed, our business could be materially and adversely affected.

A core aspect of our business is the reliability and security of our payments platform. Any perceived or actual breach of security, regardless of how it occurs or the extent of the breach, could have a significant impact on our reputation as a trusted brand, cause us to lose existing sellers, prevent us from obtaining new sellers, require us to expend significant funds to remedy problems caused by breaches and to implement measures to prevent further breaches, and expose us to legal risk and potential liability including those resulting from governmental or regulatory investigations, class action litigation and costs associated with remediation, such as fraud monitoring. Any actual or perceived security breach at a company providing services to us or our customers could have similar effects. Further, any actual or perceived security breach with respect to the bitcoin and blockchain ledger, regardless of whether such breach directly affects our products and services, could have negative reputational effects and harm customer trust in us and our products and services.

Our risk management efforts may not be effective, which could expose us to losses and liability and otherwise harm our business.

We offer managed payments and other products and services to a large number of customers, and we are responsible for vetting and monitoring these customers and determining whether the transactions we process for them are legitimate. When our products and services are used to process illegitimate transactions, and we settle those funds to sellers and are unable to recover them, we suffer losses and liability. These types of illegitimate transactions can also expose us to governmental and regulatory sanctions as well as potentially prevent us from satisfying our contractual obligations to our third party partners, which may cause us to be in breach of our obligations. The highly automated nature of, and liquidity offered by, our payments services make us a target for illegal or improper uses, including fraudulent or illegal sales of goods or services, money laundering, and terrorist financing. Identity thieves and those committing fraud using stolen or fabricated credit card or bank account numbers, or other deceptive or malicious practices, potentially can steal significant amounts of money from businesses like ours. In configuring our payments services, we face an inherent trade-off between security and customer convenience. Our risk management policies, procedures, techniques, and processes may not be sufficient to identify all of the risks to which we are exposed, to enable us to prevent or mitigate the risks we have identified, or to identify additional risks to which we may become subject in the future. As a greater number of larger sellers use our services, our exposure to material risk losses from a single seller, or from a small number of sellers, will increase. Our current business and anticipated domestic and international growth will continue to place significant demands on our risk management and compliance efforts, and we will need to continue developing and improving our existing risk management infrastructure, techniques, and processes. In addition, when we introduce new services, expand existing services including online payment acceptance, focus on new business types, or begin to operate in markets where we have a limited history of fraud loss, we may be less able to forecast and carry appropriate reserves in our books for those losses. Furthermore, if our risk management policies and processes contain errors or are otherwise ineffective, we may suffer large financial losses, we may be subject to civil and criminal liability, and our business may be materially and adversely affected.

We are currently, and will continue to be, exposed to risks associated with chargebacks and refunds in connection with payment card fraud or relating to the goods or services provided by our sellers. In the event that a billing dispute between a cardholder and a seller is not resolved in favor of the seller, including in situations where the seller engaged in fraud, the transaction is typically “charged back” to the seller and the purchase price is credited or otherwise refunded to the cardholder. If we are unable to collect chargebacks or refunds from the seller’s account, or if the seller refuses to or is unable to reimburse us for chargebacks or refunds due to closure, bankruptcy, or other reasons, we may bear the loss for the amounts paid to the cardholder. Since October 2015, businesses that cannot process EMV chip cards are held financially responsible for certain fraudulent transactions conducted using chip-enabled cards. This has shifted an increased amount of the risk for certain fraudulent transactions from the issuing banks to these sellers, which has resulted in our having to seek an increased level of reimbursement for chargebacks from our sellers that do not deploy EMV-compliant card readers. Not all of the readers we offer to merchants are EMV-compliant. Our financial results would be adversely affected to the extent sellers do not fully reimburse us for the related chargebacks. We do not collect and maintain reserves from our sellers to cover these potential losses, and for customer relations purposes we sometimes decline to seek reimbursement for certain chargebacks. The risk of chargebacks is typically greater with those of our sellers that promise future delivery of goods and services, which we allow on our Square platform. If we are unable to maintain our losses from chargebacks at acceptable levels, the payment card networks could fine us, increase our transaction-based fees, or terminate our ability to process payment cards. Any increase in our transaction-based fees could damage our business, and if we were unable to accept payment cards, our business would be materially and adversely affected.

We derive a significant portion of our revenue from managed payments services. Our efforts to expand our product portfolio and market reach may not succeed and may reduce our revenue growth.

We derive a significant portion of our revenue from transaction-based fees we collect in connection with managed payments services. While we intend to continue to broaden the scope of products and services we offer, we may not be successful in deriving any significant revenue from these products and services. Failure to broaden the scope of products and services that are attractive may inhibit the growth of repeat business and harm our business, as well as increase the vulnerability of our core payments business to competitors offering a full suite of products and services. Furthermore, we may have limited or no experience in our newer markets. For example, we cannot assure you that any of our products or services outside of managed payments services will be as widely accepted or that they will continue to grow in revenue. These offerings may present new and difficult technological, operational, regulatory and other challenges, and if we experience service disruptions, failures, or other issues, our business may be materially and adversely affected. Our newer activities may not recoup our investments in a timely manner or at all. If any of this were to occur, it could damage our reputation, limit our growth, and materially and adversely affect our business.

Our success depends on our ability to develop products and services to address the rapidly evolving market for payments and point-of-sale, financial, and marketing services, and, if we are not able to implement successful enhancements and new features for our products and services, our business could be materially and adversely affected.

We expect that new services and technologies applicable to the industries in which we operate will continue to emerge and evolve. Rapid and significant technological changes continue to confront the industries in which we operate, including developments in omnichannel commerce, proximity payment devices (including contactless payments via NFC technology), as well as developments in cryptocurrencies and in tokenization, which replaces sensitive data (e.g., payment card information) with symbols (tokens) to keep the data safe in the event that it ends up in the wrong hands.

These new services and technologies may be superior to, impair, or render obsolete the products and services we currently offer or the technologies we currently use to provide them. Incorporating new technologies into our products and services may require substantial expenditures and take considerable time, and we may not be successful in realizing a return on these development efforts in a timely manner or at all. There can be no assurance that any new products or services we develop and offer to our customers will achieve significant commercial acceptance. Our ability to develop new products and services may be inhibited by industry-wide standards, payment card networks, existing and future laws and regulations, resistance to change from our customers, which includes our sellers and their buyers, or third parties' intellectual property rights. Our success will depend on our ability to develop new technologies and to adapt to technological changes and evolving industry standards. If we are unable to provide enhancements and new features for our products and services or to develop new products and services that achieve market acceptance or that keep pace with rapid technological developments and evolving industry standards, our business would be materially and adversely affected.

The success of enhancements, new features, and products and services depends on several factors, including the timely completion, introduction, and market acceptance of the enhancements or new features, products or services. We often rely not only on our own initiatives and innovations, but also on third parties, including some of our competitors, for the development of and access to new technologies and development of a robust market for these new products and technologies. Failure to accurately predict or to respond effectively to developments in our industry may significantly impair our business.

In addition, because our products and services are designed to operate with a variety of systems, infrastructures, and devices, we need to continuously modify and enhance our products and services to keep pace with changes in mobile, software, communication, and database technologies. We may not be successful in either developing these modifications and enhancements or in bringing them to market in a timely and cost-effective manner. Any failure of our products and services to continue to operate effectively with third-party infrastructures and technologies could reduce the demand for our products and services, result in dissatisfaction of our customers, and materially and adversely affect our business.

Substantial and increasingly intense competition in our industry may harm our business.

We compete in markets characterized by vigorous competition, changing technology, changing customer needs, evolving industry standards, and frequent introductions of new products and services. We expect competition to intensify in the future as existing and new competitors introduce new services or enhance existing services. We compete against many companies to attract customers, and some of these companies have greater financial resources and substantially larger bases of customers than we do, which may provide them with significant competitive advantages. These companies may devote greater resources to the development, promotion, and sale of products and services, and they may offer lower prices or more effectively introduce their own innovative products and services that adversely impact our growth. Mergers and acquisitions by these companies may lead to even larger competitors with more resources. We also expect new entrants to offer competitive products and services. Certain sellers have long-standing exclusive, or nearly exclusive, relationships with our competitors to accept payment cards and other services that we offer. These relationships may make it difficult or cost-prohibitive for us to conduct material amounts of business with them. Competing services tied to established brands may engender greater confidence in the safety and efficacy of their services. If we are unable to differentiate ourselves from and successfully compete with our competitors, our business will be materially and adversely affected.

We may also face pricing pressures from competitors. Some potential competitors are able to offer lower prices to sellers for similar services by cross-subsidizing their payments services through other services they offer. Such competition may result in the need for us to alter the pricing we offer to our sellers and could reduce our gross profit. In addition, as we grow, sellers may demand more customized and favorable pricing from us, and competitive pressures may require us to agree to such pricing, further reducing our gross profit. We currently negotiate pricing discounts and other incentive arrangements with certain large sellers to increase acceptance and usage of our products and services. If we continue this practice and if an increasing proportion of our sellers are large sellers, we may have to increase the discounts or incentives we provide, which could also reduce our gross profit.

We are dependent on payment card networks and acquiring processors, and any changes to their rules or practices could harm our business.

Our business depends on our ability to accept credit and debit cards, and this ability is provided by the payment card networks, including Visa, MasterCard, American Express, and Discover. In a majority of these cases, we do not directly access the payment card networks that enable our acceptance of payment cards. As a result, we must rely on banks and acquiring processors to process transactions on our behalf. Our acquiring processor agreements have terms ranging from two to six years. Our three largest such agreements expire between the first quarter of 2020 and the third quarter of 2022. These banks and acquiring processors may fail or refuse to process transactions adequately, may breach their agreements with us, or may refuse to renegotiate or renew these agreements on commercially reasonable terms. They might also take actions that degrade the functionality of our services, impose additional costs or requirements on us, or give preferential treatment to competitive services, including their own services. If we are unsuccessful in establishing, renegotiating or maintaining mutually beneficial relationships with these payment card networks, banks, and acquiring processors, our business may be harmed.

The payment card networks and our acquiring processors require us to comply with payment card network operating rules, including special operating rules that apply to us as a “payment facilitator” providing payment processing services to merchants. The payment card networks set these network rules and have discretion to interpret the rules and change them at any time. Any changes to or interpretations of the network rules that are inconsistent with the way we or our acquiring processors currently operate may require us to make changes to our business that could be costly or difficult to implement. If we fail to make such changes or otherwise resolve the issue with the payment card networks, the networks could fine us or prohibit us from processing payment cards. In addition, violations of the network rules or any failure to maintain good relationships with the payment card networks could impact our ability to receive incentives from them, could increase our costs, or could otherwise harm our business. If we were unable to accept payment cards or were limited in our ability to do so, our business would be materially and adversely affected.

We are required to pay interchange and assessment fees, processing fees and bank settlement fees to third-party payment processors and financial institutions. From time to time, payment card networks have increased, and may increase in the future, the interchange fees and assessments that they charge for each transaction processed using their networks. In addition, our acquiring processors and payment card networks may refuse to renew our agreements with them on commercially reasonable terms or at all. Interchange fees or assessments are also subject to change from time to time due to government regulation. Because we generally charge our sellers a flat rate for our managed payments services, rather than passing through interchange fees and assessments to our sellers directly, any increase or decrease in interchange fees or assessments or in the fees we pay to our acquiring processors could make our pricing look less competitive, lead us to change our pricing model, or adversely affect our margins.

We could be, and in the past have been, subject to penalties from payment card networks if we fail to detect that sellers are engaging in activities that are illegal, contrary to the payment card network operating rules, or considered “high risk.” We must either prevent high-risk sellers from using our products and services or register such sellers with the payment card networks and conduct additional monitoring with respect to such sellers. Although the amount of these penalties has not been material to date, any additional penalties in the future could become material and could result in termination of our ability to accept payment cards or could require changes in our process for registering new sellers. This could materially and adversely affect our business.

Our quarterly results of operations and operating metrics fluctuate significantly and are unpredictable and subject to seasonality, which could result in the trading price of our Class A common stock being unpredictable or declining.

Our quarterly results of operations have historically fluctuated significantly and are not necessarily an indication of future performance. These fluctuations may be due to a variety of factors, some of which are outside of our control and may not fully reflect the underlying performance of our business. Our limited operating history combined with the rapidly evolving markets in which we operate also contributes to these fluctuations. Fluctuations in quarterly results may materially and adversely affect the predictability of our business and the price of our Class A common stock.

Factors that may cause fluctuations in our quarterly financial results include our ability to attract and retain new customers; seasonality in our business or our sellers' business, including seasonal fluctuations in the amount of transactions our sellers are processing; the timing, effectiveness, and costs of expansion and upgrades of our systems and infrastructure, as well as the success of those expansions and upgrades; the outcomes of legal proceedings and claims; our ability to maintain or increase revenue, gross margins, and operating margins; our ability to continue introducing new products and services and to continue convincing customers to adopt additional offerings; increases in and timing of expenses that we may incur to grow and expand our operations and to remain competitive, including strategic transactions and related transaction and integration costs; period-to-period volatility related to fraud and risk losses; system failures resulting in the inaccessibility of our products and services; changes in the regulatory environment, including with respect to security, privacy, data protection or enforcement of laws and regulations by regulators, including fines, orders, or consent decrees; changes in global business or macroeconomic conditions; unusual weather conditions or natural disasters; general retail buying patterns; and the other risks described in this Quarterly Report on Form 10-Q.

We depend on key management, as well as our experienced and capable employees, and any failure to attract, motivate, and retain our employees could harm our ability to maintain and grow our business.

Our future success is significantly dependent upon the continued service of our executives and other key employees. If we lose the services of any member of management or any key personnel, we may not be able to locate a suitable or qualified replacement, and we may incur additional expenses to recruit and train a replacement, which could severely disrupt our business and growth. Jack Dorsey, our co-founder, President, and Chief Executive Officer, also serves as Chief Executive Officer of Twitter, Inc. This may at times adversely affect his ability to devote time, attention, and effort to Square.

To maintain and grow our business, we will need to identify, hire, develop, motivate, and retain highly skilled employees. Identifying, recruiting, training, integrating, and retaining qualified individuals requires significant time, expense, and attention. In addition, from time to time, there may be changes in our management team that may be disruptive to our business. If our management team, including any new hires that we make, fails to work together effectively and to execute our plans and strategies on a timely basis, our business could be harmed. Competition for highly skilled personnel is intense, particularly in the San Francisco Bay Area where our headquarters are located. We may need to invest significant amounts of cash and equity to attract and retain new employees, and we may never realize returns on these investments. Additionally, potential changes in U.S. immigration policy may make it difficult to renew or obtain visas for any highly skilled personnel that we have hired or are actively recruiting. Negative sentiments towards the United States as a result of these potential changes may also adversely affect our international recruiting efforts. Furthermore, our international expansion and our business in general may be materially adversely affected if legislative or administrative changes to immigration or visa laws and regulations impair our hiring processes or projects involving personnel who are not citizens of the country where the work is to be performed. If we are not able to add and retain employees effectively, our ability to achieve our strategic objectives will be adversely affected, and our business and growth prospects will be harmed.

If we do not continue to improve our operational, financial and other internal controls and systems to manage growth effectively, our business could be harmed.

Our current business and anticipated growth will continue to place significant demands on our management and other resources. In order to manage our growth effectively, we must continue to strengthen our existing infrastructure and operational procedures, enhance our internal controls and reporting systems, and ensure we timely and accurately address issues as they arise. In particular, our continued growth will increase the challenges involved in:

- improving and implementing existing and developing new internal administrative infrastructure, particularly our operational, financial, communications and other internal systems and procedures;
- installing enhanced management information and control system; and
- preserving our core values, strategies, and goals and effectively communicating these to our employees worldwide.

If we are not successful in developing and implementing the right processes and tools to manage our enterprise, our ability to compete successfully and achieve our business objectives could be impaired.

These efforts may require substantial financial expenditures, commitments of resources, developments of our processes, and other investments and innovations. As we grow, we must balance the need for additional controls and systems with the ability to efficiently develop and launch new features for our products and services. However, it is likely that as we grow, we will not be able to launch new features, or respond to customer or market demands as quickly as a smaller, more efficient organization. If we do not successfully manage our growth, our business will suffer.

A deterioration of general macroeconomic conditions could materially and adversely affect our business and financial results.

Our performance is subject to economic conditions and their impact on levels of spending by businesses and their customers. Most of the sellers that use our services are small businesses, many of which are in the early stages of their development, and these businesses may be disproportionately adversely affected by economic downturns and may fail at a higher rate than larger or more established businesses. If spending by their customers declines, these businesses would experience reduced sales and process fewer payments with us or, if they cease to operate, stop using our products and services altogether. Small businesses frequently have limited budgets and limited access to capital, and they may choose to allocate their spending to items other than our financial or marketing services, especially in times of economic uncertainty or in recessions. In addition, if more of our sellers cease to operate, this may have an adverse impact not only on the growth of our payments services but also on our transaction and advance loss rates, and the success of our other services. For example, if sellers processing payments with us receive chargebacks after they cease to operate, we may incur additional losses. Additionally, the growth in the number of sellers qualifying for participation in the Square Capital program may slow, or business loans may be paid more slowly, or not at all. Further, our suppliers, distributors and other third party partners may suffer their own financial and economic challenges. Such suppliers and third parties may demand pricing accommodations, delay payment or become insolvent, which could harm our ability to meet end customer demands, collect revenue, or otherwise harm our business. Furthermore, our investment portfolio, which includes U.S. government and corporate securities, is subject to general credit, liquidity, market, and interest rate risks, which may be exacerbated by certain events that affect the global financial markets. If global credit and equity markets decline for extended periods, or if there is a downgrade of the securities within our portfolio, the investment portfolio may be adversely affected and we could determine that our investments have experienced an other-than-temporary decline in fair value, requiring impairment charges that could adversely affect our financial results. Thus, if general macroeconomic conditions deteriorate, our business and financial results could be materially and adversely affected.

We are also monitoring developments related to the decision by the U.K. government to leave the European Union (EU) following a referendum in June 2016 in which voters in the United Kingdom approved an exit from the EU (often referred to as "Brexit"), which could have significant implications for our business. In March 2017, the United Kingdom began the official process to leave the EU by April 2019. Brexit could lead to economic and legal uncertainty, including significant volatility in global stock markets and currency exchange rates, and increasingly divergent laws, regulations and licensing requirements for the Company as the United Kingdom determines which EU laws to replace or replicate. Any of these effects of Brexit, among others, could adversely affect our operations and financial results.

Expanding our business globally could subject us to new challenges and risks.

We currently offer our services and products in multiple countries and plan to continue expanding our business further globally. Expansion, whether in our existing or new global markets, will require additional resources and controls, and offering our services in new geographic regions often requires substantial expenditures and takes considerable time. We may not be successful enough in these new geographies to recoup our investments in a timely manner or at all. Such expansion could also subject our business to substantial risks, including:

- difficulty in attracting a sufficient number of sellers;
- failure to anticipate competitive conditions;
- conformity with applicable business customs, including translation into foreign languages and associated expenses;
- increased costs and difficulty in protecting intellectual property and sensitive data;
- changes to the way we do business as compared with our current operations or a lack of acceptance of our products and services;
- the ability to support and integrate with local third-party service providers;
- competition with service providers or other entrenched market-players that have greater experience in the local markets than we do;
- difficulties in staffing and managing foreign operations in an environment of diverse culture, laws and customs, challenges caused by distance, language, and cultural differences, and the increased travel, infrastructure and legal and compliance costs associated with global operations;
- difficulties in recruiting and retaining qualified employees and maintaining our company culture;
- difficulty in gaining acceptance from industry self-regulatory bodies;

- compliance with multiple, potentially conflicting and changing governmental laws and regulations, including with respect to data privacy, data protection and information security;
- compliance with U.S. and foreign anti-corruption, anti-bribery and anti-money laundering laws;
- potential tariffs, sanctions, fines or other trade barriers;
- exchange rate risk;
- compliance with potentially conflicting and changing laws of taxing jurisdictions where we conduct business and applicable U.S. tax laws, the complexity and adverse consequences of such tax laws and potentially adverse tax consequences due to changes in such tax laws; and
- regional economic and political instability.

As a result of these risks, our efforts to expand our global operations may not be successful, which could limit our ability to grow our business.

Any acquisitions, strategic investments, entries into new businesses, divestitures, and other transactions could fail to achieve strategic objectives, disrupt our ongoing operations, harm our business and negatively impact our results of operations.

In pursuing our business strategy, we routinely conduct discussions and evaluate opportunities for possible acquisitions, strategic investments, entries into new businesses, divestitures, and other transactions. We have in the past acquired, and we continue to seek to acquire or invest in businesses, apps, or technologies that we believe could complement or expand our products and services, enhance our technical capabilities, or otherwise offer growth opportunities. The identification, evaluation, and negotiation of potential acquisitions or divestitures may divert the attention of management and entail various expenses, whether or not such transactions are ultimately completed. We also have limited experience in acquiring other businesses. In addition to transaction and opportunity costs, these transactions involve large challenges and risks, whether or not such transactions are completed, any of which could harm our business and negatively impact our results of operations, including risks that:

- the transaction may not advance our business strategy;
- we may spend time and resources on opportunities that we are unable to consummate on terms acceptable to us;
- the transaction may not close or may be delayed;
- we may not be able to secure required regulatory approvals or otherwise satisfy closing conditions for a proposed transaction in a timely manner, or at all;
- we may not realize a satisfactory return or increase our revenue;
- we may experience difficulty, and may not be successful in, integrating the acquired business and we may not realize the expected synergies of the transaction in a timely manner, or at all;
- we may incur significant acquisition costs and transition costs;
- we may experience disruptions on our ongoing operations and divert management's attention;
- we may not realize the expected benefits from the transaction in the expected time period, or at all;
- we may be unable to retain key personnel;
- we may experience difficulty and may not be successful in integrating technologies, IT systems, accounting systems, culture, or personnel;
- acquired businesses may not have adequate controls, processes and procedures to ensure compliance with laws and regulations, and our due diligence process may not identify compliance issues or other liabilities;
- we may incur substantial liabilities, whether known or unknown, associated with the transaction;

we may assume additional financial or legal exposure, including exposure that is known to us;
we may have difficulty entering new market segments;
we may be unable to retain the customers and partners of acquired businesses;
there may be unknown, underestimated, or undisclosed commitments or liabilities, including actual or threatened litigation;
there may be regulatory constraints, particularly competition regulations that may affect the extent to which we can maximize the value of our acquisitions or investments;
acquisitions could result in dilutive issuances of equity securities or the incurrence of debt; and
our business, the acquired business, or the integrated business may be adversely affected by other political, business, and general economic conditions.;

We may also choose to divest certain businesses or product lines that no longer fit with our strategic objectives. If we decide to sell assets or a business, we may have difficulty obtaining terms acceptable to us in a timely manner, or at all. Additionally, we may experience difficulty separating out portions of or entire businesses, incur potential loss of revenue or experience negative impact on margins. Such potential transactions may also delay achievement of our strategic objectives, cause us to incur additional expenses, potentially disrupt seller relationships, and expose us to unanticipated or ongoing obligations and liabilities.

We rely on third parties and their systems for a variety of services, including the processing of transaction data and settlement of funds to us and our sellers, and these third parties' failure to perform these services adequately could materially and adversely affect our business.

To provide our managed payments solution and other products and services, we rely on third parties that we do not control, such as the payment card networks, our acquiring processors, the payment card issuers, various financial institution partners (including those for Square Capital and Cash App), systems like the Federal Reserve Automated Clearing House, and other partners. We rely on these third parties for a variety of services, including the transmission of transaction data, processing of chargebacks and refunds, settlement of funds to our sellers, and the provision of information and other elements of our services. For example, we currently rely on three acquiring processors in the United States, Canada and Japan and two for each of Australia and the United Kingdom. While we believe there are other acquiring processors that could meet our needs, adding or transitioning to new providers may significantly disrupt our business and increase our costs. In the event these third parties fail to provide these services adequately, including as a result of financial difficulty or insolvency, errors in their systems or events beyond their control, or refuse to provide these services on terms acceptable to us or at all, and we are not able to find suitable alternatives, our business may be materially and adversely affected.

In addition, we use third-party technology and systems for a variety of our day-to-day business operations. Although we have developed systems and processes that are designed to prevent data loss and other security breaches, including systems and processes designed to reduce the impact of a security breach at a third-party vendor, such measures cannot provide absolute security.

Our services must integrate with a variety of operating systems, and the hardware that enables merchants to accept payment cards must interoperate with third-party mobile devices utilizing those operating systems. If we are unable to ensure that our services or hardware interoperate with such operating systems and devices, our business may be materially and adversely affected.

We are dependent on the ability of our products and services to integrate with a variety of operating systems, as well as web browsers that we do not control. Any changes in these systems that degrade the functionality of our products and services, impose additional costs or requirements on us, or give preferential treatment to competitive services, including their own services, could materially and adversely affect usage of our products and services. In addition, we rely on app marketplaces, such as the Apple App Store and Google Play, to drive downloads of our mobile app. Apple, Google, or other operators of app marketplaces regularly make changes to their marketplaces, and those changes may make access to our products and services more difficult. In the event that it is difficult for our customers to access and use our products and services, our business may be materially and adversely affected. Furthermore, Apple, Google, or other operators of app marketplaces regularly provide software updates, and such software updates may not operate effectively with our products and services, which may reduce the demand for our products and services, result in dissatisfaction by our customers, and may materially and adversely affect our business.

In addition, our hardware interoperates with wired and wireless interfaces to mobile devices developed by third parties. For example, the current version of our magstripe reader plugs into the audio jack of most smartphones and tablets. In 2016, Apple introduced the iPhone 7, which does not have an audio jack, and instead Apple provided an adapter that can be inserted into a connectivity port, and subsequent models have operated the same. This change and other potential changes in the design of future mobile devices may limit the interoperability of our hardware and software with such devices and require modifications to our hardware or software. If we are unable to ensure that our hardware and software continue to interoperate effectively with such devices, if doing so is costly, or if existing merchants decide not to utilize additional parts necessary for interoperability, our business may be materially and adversely affected.

Many of our key components are procured from a single or limited number of suppliers. Thus, we are at risk of shortage, price increases, changes, delay, or discontinuation of key components, which could disrupt and materially and adversely affect our business.

Many of the key components used to manufacture our products, such as the custom parts of our magstripe reader, including its magnetic stripe-reading element, its plastic cover, and its application-specific integrated circuits, come from limited or single sources of supply, as do the plastic cover, connector, and security cage of our contactless and chip reader. In addition, in some cases, we rely only on one manufacturer to fabricate, test, and assemble our products. For example, a single manufacturer assembles our magstripe reader and our contactless and chip reader, as well as manufactures those products' plastic parts with custom tools that we own but that they maintain on their premises. The term of the agreement with that manufacturer automatically renews for consecutive one-year periods unless either party provides notice of non-renewal. In general, our contract manufacturers fabricate or procure components on our behalf, subject to certain approved procedures or supplier lists, and we do not have firm commitments from all of these manufacturers to provide all components, or to provide them in quantities and on timelines that we may require. For example, pursuant to a development and supply agreement, a component supplier provides design, development, customization, and related services for components of the magnetic stripe-reading element in some of our products. The term of the agreement renews for successive two-year terms unless either party provides notice of non-renewal. Similarly, a component provider develops certain application-specific integrated circuits for our products pursuant to our designs and specifications. The term of our agreement with this provider renews for consecutive one-year periods unless either party provides notice of non-renewal.

Due to our reliance on the components or products produced by suppliers such as these, we are subject to the risk of shortages and long lead times in the supply of certain components or products. We are still in the process of identifying alternative manufacturers for the assembly of our products and for most of the single-sourced components used in our products. In the case of off-the-shelf components, we are subject to the risk that our suppliers may discontinue or modify them, or that the components may cease to be available on commercially reasonable terms, or at all. We have in the past experienced, and may in the future experience, component shortages or delays or other problems in product assembly, and the availability of these components or products may be difficult to predict. For example, our manufacturers may experience temporary or permanent disruptions in their manufacturing operations due to equipment breakdowns, labor strikes or shortages, natural disasters, component or material shortages, cost increases, acquisitions, insolvency, changes in legal or regulatory requirements, or other similar problems.

Additionally, various sources of supply-chain risk, including strikes or shutdowns at delivery ports or loss of or damage to our products while they are in transit or storage, intellectual property theft, losses due to tampering, third-party vendor issues with quality or sourcing control, failure by our suppliers to comply with applicable laws and regulation or other similar problems could limit or delay the supply of our products or harm our reputation. In the event of a shortage or supply interruption from suppliers of these components, we may not be able to develop alternate sources quickly, cost-effectively, or at all. Any interruption or delay in manufacturing, component supply, any increases in component costs, or the inability to obtain these parts or components from alternate sources at acceptable prices and within a reasonable amount of time, would harm our ability to provide our products to sellers on a timely basis. This could harm our relationships with our sellers, prevent us from acquiring new sellers, and materially and adversely affect our business.

Our business could be harmed if we are unable to accurately forecast demand for our products and to adequately manage our product inventory.

We invest broadly in our business, and such investments are driven by our expectations of the future success of a product. For example, our products such as the Square Reader often require investments with long lead times. An inability to correctly forecast the success of a particular product could harm our business. We must forecast inventory needs and expenses and place orders sufficiently in advance with our third-party suppliers and contract manufacturers based on our estimates of future demand for particular products. Our ability to accurately forecast demand for our products could be affected by many factors, including an increase or decrease in demand for our products or for our competitors' products, unanticipated changes in general market conditions, and the change in economic conditions.

If we underestimate demand for a particular product, our contract manufacturers and suppliers may not be able to deliver sufficient quantities of that product to meet our requirements, and we may experience a shortage of that product available for sale or distribution. The shortage of a popular product could materially and adversely affect our brand, our seller relationships, and the acquisition of additional sellers. If we overestimate demand for a particular product, we may experience excess inventory levels for that product and the excess inventory may become obsolete or out-of-date. Inventory levels in excess of demand may result in inventory write-downs or write-offs and the sale of excess inventory at further discounted prices, which could negatively impact our gross profit and our business.

Our products and services may not function as intended due to errors in our software, hardware, and systems, product defects, or due to security breaches or human error in administering these systems, which could materially and adversely affect our business.

Our software, hardware, and systems may contain undetected errors that could have a material adverse effect on our business, particularly to the extent such errors are not detected and remedied quickly. We have from time to time found defects in our customer-facing software and hardware, internal systems, and technical integrations with third-party systems, and new errors may be introduced in the future. We rely on a limited number of component and product suppliers located outside of the U.S. to manufacture our products. As a result, our direct control over production and distribution is limited and it is uncertain what effect such diminished control will have on the quality of our products. If there are defects in the manufacture of our hardware products, we may face negative publicity, government investigations, and litigation, and we may not be fully compensated by our suppliers for any financial or other liability that we suffer as a result.

In addition, we provide frequent incremental releases of product and service updates and functional enhancements, which increase the possibility of errors. The electronic payments products and services we provide are designed to process complex transactions and deliver reports and other information related to those transactions, all at high volumes and processing speeds. Since customers use our services for important aspects of their businesses, any errors, defects, security breaches such as cyber-attacks or identify theft, malfeasance, disruptions in services, or other performance problems with our services could hurt our reputation and damage our customers' businesses. Software and system errors, or human error, could delay or inhibit settlement of payments, result in oversettlement, cause reporting errors, or prevent us from collecting transaction-based fees, all of which have occurred in the past. Similarly, third-party security breaches such as cyber-attacks or identity theft could disrupt the proper functioning of our software products or services, cause errors, allow unauthorized access to sensitive, proprietary or confidential information of ours or our customers, and other destructive outcomes. Moreover, security breaches or errors in our hardware design or manufacture could cause product safety issues typical of consumer electronics devices. Such issues could lead to product recalls and inventory shortages, result in costly and time-consuming efforts to redesign and redistribute our products, give rise to regulatory inquiries and investigations, and result in lawsuits and other liabilities and losses, which could have a material and adverse effect on our business.

Additionally, electronic payment products and services, including ours, have been and could continue to be in the future, specifically targeted and penetrated or disrupted by hackers. Although these attacks on us have not been successful in disrupting our products and services thus far, our data encryption may be unable to prevent unauthorized use. Because the techniques used to obtain unauthorized access to data, products and services, and disable, alter, degrade, or sabotage them, change frequently and may be difficult to detect or remediate for long periods of time, we and our customers may be unable to anticipate these techniques or implement adequate preventative measures to stop them. If we or our sellers are unable to anticipate or prevent these attacks, our sellers' businesses may be harmed, our reputation could be damaged, and we could incur significant liability. While we maintain cybersecurity insurance, our insurance may be insufficient to cover all liabilities incurred by these attacks.

Systems failures, interruptions, delays in service, catastrophic events, and resulting interruptions in the availability of our products or services, or those of our sellers, could harm our business and our brand, and subject us to substantial liability.

Our systems and those of our third-party data center facilities may experience service interruptions, denial-of-service and other cyber-attacks and security incidents, human error, earthquakes, hurricanes, floods, fires, other natural disasters, power losses, disruptions in telecommunications services, fraud, military or political conflicts, terrorist attacks and other geopolitical unrest, computer viruses, changes in social, political or regulatory conditions or in laws and policies, or other changes or events. Our systems are also subject to break-ins, sabotage, and acts of vandalism. Some of our systems are not fully redundant, and our disaster-recovery planning is not sufficient for all eventualities. In addition, as a provider of payments solutions, we are subject to increased scrutiny by regulators that may require specific business continuity and disaster recovery plans and more rigorous testing of such plans. This increased scrutiny may be costly and time-consuming and may divert our resources from other business priorities.

We have experienced and will likely continue to experience denial-of-service attacks, system failures, and other events or conditions that interrupt the availability or reduce the speed or functionality of our products and services. These events have resulted and likely will result in loss of revenue. In addition, they could result in significant expense to repair or replace damaged equipment and remedy resultant data loss or corruption. A prolonged interruption in the availability or reduction in the speed or other functionality of our products or services could materially harm our reputation and business. Frequent or persistent interruptions in our products and services could cause customers to believe that our products and services are unreliable, leading them to switch to our competitors or to avoid our products and services, and could permanently harm our reputation and business. Moreover, to the extent that any system failure or similar event results in damages to customers or their businesses, these customers could seek compensation from us for their losses, and those claims, even if unsuccessful, would likely be time-consuming and costly for us to address.

A significant natural disaster could have a material and adverse impact on our business. Our headquarters and certain of our data center facilities are located in the San Francisco Bay Area, a region known for seismic activity. Despite any precautions we may take, the occurrence of a natural disaster or other unanticipated problems at our headquarters or data centers could result in lengthy interruptions in our services or could result in related liabilities. We have implemented a disaster recovery program, which enables us to move production to a back-up data center in the event of a catastrophe. Although this program is functional, it may prove to be inadequate, increasing the risk of interruptions in our services, which could have a material and adverse impact on our business. We do not maintain insurance sufficient to compensate us for the potentially significant losses that could result from disruptions to our services.

Significant natural or other disasters could also have a material and adverse impact on our sellers, which, in the aggregate, could in turn adversely affect our results of operations.

The loss or destruction of a private key required to access a bitcoin may be irreversible. If we are unable to access our private keys or if we experience a hack or other data loss relating to the bitcoins we hold on behalf of customers, our customers may be unable to access their bitcoins and it could harm customer trust in us and our products.

Bitcoins are controllable only by the possessor of both the unique public key and private key relating to the local or online digital wallet in which the bitcoins are held. While the bitcoin and blockchain ledger require a public key relating to a digital wallet to be published when used in a transaction, private keys must be safeguarded and kept private in order to prevent a third party from accessing the bitcoins held in such wallet. To the extent our private key is lost, destroyed or otherwise compromised and no backup of the private key is accessible, we will be unable to access the bitcoins held in the related digital wallet. Further, we cannot provide assurance that our wallet will not be hacked or compromised. The bitcoin and blockchain ledger, as well as other cryptocurrencies and blockchain technologies, have been, and may in the future be, subject to security breaches, hacking, or other malicious activities. Any loss of private keys relating to, or hack or other compromise of, digital wallets used to store our customers' bitcoins could adversely affect our customers' ability to access or sell their bitcoins and could harm customer trust in us and our products. Additionally, any loss of private keys relating to, or hack or other compromise of, digital wallets used by third parties to store bitcoins or other cryptocurrencies could have negative reputational effects on us and harm customer trust in us and our products.

Square Capital is subject to additional risks relating to the availability of capital, seller payments, availability and structure of its bank partnership, expansion of its products, and general macroeconomic conditions.

Square Capital, which includes our wholly owned subsidiary Square Capital, LLC, is subject to risks in addition to those described elsewhere in this Quarterly Report on Form 10-Q. Maintaining and growing Square Capital is dependent on institutional third-party investors purchasing the eligible business loans originated by our bank partner. If such third parties fail to continue to purchase such business loans or reduce the amount of future loans they purchase, then our bank partner may need to reduce originations, or we would need to fund the purchase of additional business loans from our own resources. We then may have to reduce the scale of Square Capital, which could have a direct impact on our ability to grow. Additionally, Square Capital has certain customary repurchase obligations in its loan purchase and servicing agreements with such institutional third party investors for breaches of certain eligibility representations and warranties. If third parties reduce the price they are willing to pay for these business loans or reduce the servicing fees they pay us in exchange for servicing the business loans on their behalf, then the financial performance of Square Capital would be harmed.

The business loans are generally unsecured obligations of our Square sellers who utilize Square Capital, and they are not guaranteed or insured in any way. Adverse changes in macroeconomic conditions or the credit quality of our Square sellers could cause some Square sellers who utilize Square Capital to cease operating or to experience a decline in their payment processing volume, thereby rendering them unable to make payment on the business loan and/or extend the repayment period beyond the contractual repayment terms on the business loan. To the extent a seller breaches a contractual obligation, such as the requirement to make minimum payments or other breach, the seller would be liable for an accelerated business loan repayment, where Square Capital's recourse is to the business and not to any individual or other asset. In addition, because the servicing fees we receive from third party investors depend on the collectability of the business loans, if there is an increase in Square sellers who utilize Square Capital who are unable to make repayment of business loans, we will be unable to collect our entire servicing fee for such loans.

In addition, adverse changes in macroeconomic conditions could lead to a decrease in the number of sellers eligible for Square Capital facilitated business loans and strain our ability to correctly identify such sellers on behalf of our bank partner or manage the risk of non-payment or fraud as servicer of the business loans. Similarly, if we fail to correctly predict the likelihood of timely repayment of the business loans or correctly price the business loans to sellers utilizing Square Capital, our business may be materially and adversely affected.

We have partnered with a Utah-chartered, member FDIC industrial bank to originate the business loans. Such bank is subject to oversight both by the FDIC and the State of Utah. Due to the fact that we are a service-provider to our bank partner, we are subject to audit standards for third-party vendors in accordance with FDIC guidance and examinations by the FDIC. There has been, and may continue to be, regulatory interest in and/or litigation challenging partnered lending arrangements where a bank makes loans and then sells and assigns such loans to a non-bank entity that is engaged in assisting with the origination and servicing of the loan. If our bank partner ceases to partner with us, ceases to abide by the terms of our agreement with them, or cannot partner with us on commercially reasonable terms, and we are not able to find suitable alternatives and/or make business loans ourselves pursuant to state licensing requirements, Square Capital may need to enter into a new partnership with another qualified financial institution, revert to the merchant cash advance (MCA) model, or pursue an alternative model for originating business loans, all of which may be time-consuming and costly and/or lead to a loss of institutional third-party investors willing to purchase such business loans or MCAs, and as a result Square Capital may be materially and adversely affected.

We intend to continue to explore other products, models and structures for Square Capital, including partnering with referral partners and forming a Utah industrial loan corporation and other forms of credit and loan origination. Some of those models or structures may require, or be deemed to require, additional procedures, partnerships, licenses, regulatory approvals or capabilities that we have not yet obtained or developed. For example, in 2017 we launched a limited consumer lending pilot program. The licenses required in connection with such pilot and other activities related to the Square Capital program subject us to reporting requirements, bonding requirements, and inspection by applicable state regulatory agencies. Should we fail to expand and evolve Square Capital in this manner, or should these new products, models or structures, or new regulations or interpretations of existing regulations, impose requirements on us that are impractical or that we cannot satisfy, the future growth and success of Square Capital may be materially and adversely affected.

Our business is subject to extensive regulation and oversight in a variety of areas, all of which are subject to change and uncertain interpretation.

We are subject to a wide variety of local, state, federal, and international laws, regulations, and industry standards in the United States and in other countries in which we operate. These laws and regulations govern numerous areas that are important to our business, including, but not limited to, consumer protection, privacy, information security, fair lending, financial services, labor and employment, immigration, import and export practices, product labeling, competition, data protection, and marketing and communications practices. Such laws and regulations are subject to changes and evolving interpretations and application, including by means of legislative changes and/or executive orders, and it can be difficult to predict how they may be applied to our business and the way we conduct our operations, particularly as we introduce new products and services and expand into new jurisdictions. Any perceived or actual breach of laws and regulations could result in investigations, regulatory inquiries, litigation, fines, or otherwise negatively impact our business. It is possible that these laws and regulations could be interpreted or applied in a manner that would prohibit, alter, or impair our existing or planned products and services; that could cause us to be subject to audits, inquiries, investigations, or lawsuits; that could result in fines, injunctive relief, or other liabilities; or that could require costly, time-consuming, or otherwise burdensome compliance measures from us.

In particular, as we seek to build a trusted and secure platform for commerce, and as we expand our network of customers and facilitate their transactions and interactions with one another or otherwise evolve our products and services, we will increasingly be subject to laws and regulations relating to the collection, use, retention, privacy, security, and transfer of information, including the personally identifiable information of our employees and customers. As with the other laws and regulations noted above, these laws and regulations may change or be interpreted and applied differently over time and from jurisdiction to jurisdiction, and it is possible they will be interpreted and applied in ways that will materially and adversely affect our business. For example, the European Parliament and the Council of the European Union in 2016 adopted a General Data Protection Regulation (GDPR), effective in May 2018, that will supersede current EU data protection legislation, impose more stringent data privacy and data protection requirements and provide greater penalties for noncompliance of up to the greater of 4% of worldwide annual revenue or €20 million. In the United Kingdom, a Data Protection Bill that proposes to substantially implement the GDPR has progressed through Parliament and is expected to become law in May 2018. Nevertheless, the Data Protection Bill must complete the legislative process, and a number of amendments have been proposed so it remains unclear what modifications will be made to the final legislation or how it will be interpreted once enacted. In addition, U.S. and international laws that have been applied to protect user privacy (including laws regarding unfair and deceptive practices in the U.S. and GDPR in the EU) may be subject to evolving interpretations or applications in light of privacy developments.

We have incurred, and may continue to incur, significant expenses to comply with mandatory privacy and security standards and protocols imposed by law, regulation, industry standards or contractual obligations. We post on our website our privacy policies and practices concerning the collection, use, and disclosure of information. Any failure, real or perceived, by us to comply with our posted privacy policies or with any regulatory requirements or orders, other local, state, federal, or international privacy, data protection, information security or consumer protection-related laws and regulations, industry standards or contractual obligations could cause our customers to reduce their use of our products and services and could materially and adversely affect our business.

Further, from time to time, we may leverage third parties to help conduct our businesses in the U.S. or abroad. We and our third-party intermediaries may have direct or indirect interactions with officials and employees of government agencies or state-owned or affiliated entities and may be held liable for the corrupt or other illegal activities of these third-party business partners and intermediaries, our employees, representatives, contractors, channel partners, and agents, even if we do not explicitly authorize such activities. While we have policies and procedures to address compliance with such laws, we cannot assure you that all of our employees and agents will not take actions in violation of our policies and applicable law, for which we may be ultimately held responsible.

We may not be able to respond quickly or effectively to regulatory, legislative and other developments, and these changes may in turn impair our ability to offer our existing or planned features, products and services and/or increase our cost of doing business. In addition, if our practices are not consistent or viewed as not consistent with the legal and regulatory requirements, including changes in laws and regulations or new interpretations of existing laws and regulations, we may become subject to audits, inquiries, whistleblower complaints, adverse media coverage, investigations, loss of export privileges, severe criminal or civil sanctions, or suspension or debarment from U.S. government contracts, all of which may have an adverse effect on our reputation, our business, results of operations and financial condition.

Our business is subject to complex and evolving regulations and oversight related to our provision of payments services and other financial services.

The state and federal laws, rules, regulations, and licensing schemes that govern our business include or may in the future include those relating to banking, lending, deposit-taking, cross-border and domestic money transmission, foreign exchange, payments services (such as payment processing and settlement services), cryptocurrency, consumer financial protection, anti-money laundering, escheatment, international sanctions regimes, and compliance with the Payment Card Industry Data Security Standard, a set of requirements designed to ensure that all companies that process, store, or transmit payment card information maintain a secure environment to protect cardholder data. These laws, rules, and regulations are enforced by multiple authorities and governing bodies in the United States, including the Department of the Treasury, the Consumer Financial Protection Bureau, the Federal Deposit Insurance Corporation, and numerous state and local agencies. Outside of the United States, we are subject to additional laws, rules, and regulations related to the provision of payments and financial services, including those enforced by the Ministry of Economy, Trade, and Industry in Japan, those enforced by the Australian Transaction Reports and Analysis Centre, and those enforced by the Financial Conduct Authority in the United Kingdom. As we expand into new jurisdictions, the number of foreign regulations and regulators governing our business will expand as well. If we pursue additional or alternative means of growing Square Capital, additional state and federal regulations would apply. Similarly, if we choose to offer Square Payroll in more jurisdictions, additional regulations, including tax rules, will apply. In addition, as our business and products continue to develop and expand, we may become subject to additional rules and regulations.

We recently introduced a feature to the Cash App that permits our customers to buy and sell bitcoin. Bitcoin is not considered legal tender or backed by any government, and it has experienced price volatility, technological glitches and various law enforcement and regulatory interventions. We do not believe that the bitcoin platform involves offering securities that are subject to the registration or other provisions of the federal or state securities laws. We also do not believe the feature subjects us to regulation under the federal securities laws, including as a broker-dealer or an investment adviser, or registration under the federal commodities laws. However, the regulation of cryptocurrency and crypto platforms is still an evolving area and it is possible that a court or a federal or state regulator could disagree with one or more of these conclusions. If we fail to comply with regulations or prohibitions applicable to us, we could face regulatory or other enforcement actions and potential fines and other consequences. Further, we might not be able to continue operating the feature, at least in current form, and to the extent that the feature is viewed by the market as a valuable asset to Square, the price of our Class A common stock could decrease.

Although we have a compliance program focused on the laws, rules, and regulations applicable to our business and we are continually investing more in this program, we may still be subject to fines or other penalties in one or more jurisdictions levied by federal, state or local regulators, including state Attorneys General and private plaintiffs who may be acting as private attorneys general pursuant to various applicable federal, state and local laws, as well as those levied by foreign regulators. In addition to fines, penalties for failing to comply with applicable rules and regulations could include significant criminal and civil lawsuits, forfeiture of significant assets, increased licensure requirements, or other enforcement actions. We could also be required to make changes to our business practices or compliance programs as a result of regulatory scrutiny. In addition, any perceived or actual breach of compliance by us with respect to applicable laws, rules, and regulations could have a significant impact on our reputation as a trusted brand and could cause us to lose existing customers, prevent us from obtaining new customers, require us to expend significant funds to remedy problems caused by breaches and to avert further breaches, and expose us to legal risk and potential liability.

We have obtained licenses to operate as a money transmitter (or its equivalent) in the United States and in the states where this is required. As a licensed money transmitter, we are subject to obligations and restrictions with respect to the investment of customer funds, reporting requirements, bonding requirements, and inspection by state regulatory agencies concerning those aspects of our business considered money transmission. Evaluation of our compliance efforts, as well as the questions of whether and to what extent our products and services are considered money transmission, are matters of regulatory interpretation and could change over time. In the past, we have been subject to fines and other penalties by regulatory authorities due to their interpretations and applications to our business of their respective state money transmission laws. In the future, as a result of the regulations applicable to our business, we could be subject to investigations and resulting liability, including governmental fines, restrictions on our business, or other sanctions, and we could be forced to cease conducting certain aspects of our business with residents of certain jurisdictions, be forced to otherwise change our business practices in certain jurisdictions, or be required to obtain additional licenses or regulatory approvals. There can be no assurance that we will be able to obtain any such licenses, and, even if we were able to do so, there could be substantial costs and potential product changes involved in maintaining such licenses, which could have a material and adverse effect on our business.

We are subject to risks related to litigation, including intellectual property claims, government investigations or inquiries, and regulatory matters or disputes.

We may be, and have been, subject to claims, lawsuits (including class actions and individual lawsuits), government or regulatory investigations, subpoenas, inquiries or audits, and other proceedings involving intellectual property, consumer protection, privacy, data protection, labor and employment, immigration, import and export practices, product labeling, competition, accessibility, securities, tax, marketing and communications practices, commercial disputes, anti-money laundering, anti-corruption, counter-terrorist financing, sanctions, and other matters.

The number and significance of our legal disputes and inquiries have increased as we have grown larger, as our business has expanded in scope and geographic reach, and as our products and services have increased in complexity, and we expect that we will continue to face additional legal disputes as we continue to grow and expand.

We receive significant media attention and, as a public company, have a higher profile, which could result in increased litigation or other legal or regulatory proceedings. In addition, some of the laws and regulations affecting the internet, mobile commerce, payment processing, business financing, and employment did not anticipate businesses like ours, and many of the laws and regulations, including those affecting us have been enacted relatively recently. As a result, there is substantial uncertainty regarding the scope and application of many of the laws and regulations to which we are subject, which increases the risk that we will be subject to claims alleging violations of those laws and regulations. We may also be accused of having, or be found to have, infringed or violated third-party intellectual property rights.

The scope, outcome and impact of claims, lawsuits, government or regulatory investigations, subpoenas, inquiries or audits and other proceedings to which we are subject cannot be predicted with certainty. Regardless of the outcome, such investigations and legal proceedings can have a material and adverse impact on us due to their costs, diversion of our resources, and other factors. Plaintiffs may seek, and we may become subject to, preliminary or provisional rulings in the course of litigation, including preliminary injunctions requiring us to cease some or all of our operations. We may decide to settle legal disputes on terms that are unfavorable to us. Furthermore, if any litigation to which we are a party is resolved adversely, we may be subject to an unfavorable judgment that we may not choose to appeal or that may not be reversed upon appeal. We may have to seek a license to continue practices found to be in violation of a third party’s rights, or we may have to change or cease certain practices. If we are required, or choose to enter into, royalty or licensing arrangements, such arrangements may not be available on reasonable terms or at all and may significantly increase our operating costs and expenses. As a result, we may also be required to develop or procure alternative non-infringing technology or discontinue use of technology, and doing so could require significant effort and expense or may not be feasible. In addition, the terms of any settlement or judgment in connection with any legal claims, lawsuits, or proceedings may require us to cease some or all of our operations or pay substantial amounts to the other party and could materially and adversely affect our business.

Our intellectual property rights are valuable, and any inability to protect them could reduce the value of our products, services, and brand.

Our trade secrets, trademarks, copyrights, patents, and other intellectual property rights are critical to our success. We rely on, and expect to continue to rely on, a combination of confidentiality, invention assignment, and license agreements with our employees, consultants, and third parties with whom we have relationships, as well as trademark, trade dress, domain name, copyright, trade secret, and patent rights, to protect our brand and other intellectual property rights. However, various events outside of our control may pose a threat to our intellectual property rights, as well as to our products and services. Effective protection of trademarks, copyrights, domain names, patent rights, and other intellectual property rights is expensive and difficult to maintain, both in terms of application and maintenance costs, as well as the costs of defending and enforcing those rights. The efforts we have taken to protect our intellectual property rights may not be sufficient or effective. Our intellectual property rights may be infringed, misappropriated, or challenged, which could result in them being narrowed in scope or declared invalid or unenforceable. Similarly, our reliance on unpatented proprietary information and technology, such as trade secrets and confidential information, depends in part on agreements we have in place with employees and third parties that place restrictions on the use and disclosure of this intellectual property. These agreements may be insufficient or may be breached, or we may not enter into sufficient agreements with such individuals in the first instance, in either case potentially resulting in the unauthorized use or disclosure of our trade secrets and other intellectual property, including to our competitors, which could cause us to lose any competitive advantage resulting from this intellectual property. Individuals not subject to invention assignment agreements may make adverse ownership claims to our current and future intellectual property. There can be no assurance that our intellectual property rights will be sufficient to protect against others offering products or services that are substantially similar to ours and that compete with our business.

As of March 31, 2018, we had 424 issued patents in force in the United States and abroad and 606 filed patent applications pending in the United States and abroad, though there can be no assurance that any or all of these pending applications will ultimately be issued as patents. We also pursue registration of copyrights, trademarks, and domain names in the United States and in certain jurisdictions outside of the United States, but doing so may not always be successful or cost-effective. In general, we may be unable or, in some instances, choose not to obtain legal protection for our intellectual property, and our existing and future intellectual property rights may not provide us with competitive advantages or distinguish our products and services from those of our competitors. The laws of some foreign countries do not protect our intellectual property rights to the same extent as the laws of the United States, and effective intellectual property protection and mechanisms may not be available in those jurisdictions. We may need to expend additional resources to defend our intellectual property in these countries, and the inability to do so could impair our business or adversely affect our international expansion. Our intellectual property rights may be contested, circumvented, or found unenforceable or invalid, and we may not be able to prevent third parties from infringing, diluting, or otherwise violating them.

Additionally, our intellectual property rights and other confidential business information is subject to risks of compromise or unauthorized disclosure if our security measures are unable to prevent cyber attacks. Our security measures, including those of our third-party service providers, may not detect or prevent all attempted security breaches or other attacks that may jeopardize the security of information stored in or transmitted by our systems or those of our third-party service providers. Such attacks could lead to the loss of critical data or the unauthorized disclosure or use of our proprietary information and other confidential information. Any such attacks, or the perception that such attacks have occurred, could negatively impact our ability to protect our intellectual property rights, our reputation, or customer trust in us and our products.

Significant impairments of our intellectual property rights, and limitations on our ability to assert our intellectual property rights against others, could have a material and adverse effect on our business.

We may not be able to secure financing on favorable terms, or at all, to meet our future capital needs and our existing credit facility contains, and any future debt financing may contain, covenants that impact the operation of our business and pursuit of business opportunities.

We have funded our operations since inception primarily through debt and equity financings, bank credit facilities, and capital lease arrangements. While we believe that our existing cash and cash equivalents, marketable securities, and availability under our line of credit are sufficient to meet our working capital needs and planned capital expenditures, and service our debt, there is no guarantee that this will continue to be true in the future. In the future, we may require additional capital to respond to business opportunities, refinancing needs, business and financial challenges, regulatory surety bond requirements, acquisitions, or unforeseen circumstances and may decide to engage in equity, equity-linked, or debt financings or enter into additional credit facilities for other reasons, and we may not be able to secure any such additional financing or refinancing on favorable terms, in a timely manner, or at all. If we are unable to obtain adequate financing or financing on terms satisfactory to us when we require it, our ability to continue to grow or support our business and to respond to business challenges could be significantly limited.

Our credit facility contains affirmative and negative covenants, including customary limitations on the incurrence of certain indebtedness and liens, restrictions on certain inter-company transactions, and limitations on dividends and stock repurchases. Any debt financing obtained by us in the future could also involve restrictive covenants relating to our capital-raising activities and other financial and operational matters, which may make it more difficult for us to operate our business, obtain additional capital, and pursue business opportunities, including potential acquisitions. Our ability to comply with these covenants may be affected by events beyond our control, and breaches of these covenants could result in a default under our existing credit facility and any future financing agreements into which we may enter. If not waived, these defaults could cause indebtedness outstanding under our credit facility and any future financing agreements that we may enter into to become immediately due and payable, which event may also constitute a default under our other indebtedness, including our 0.375% convertible senior notes due 2022 (Notes).

If we raise additional funds through further issuances of equity or other securities convertible into equity, including convertible debt securities, our existing stockholders could suffer dilution in their percentage ownership of our company, and any such securities we issue could have rights, preferences, and privileges senior to those of holders of our Class A common stock.

Servicing our Notes may require a significant amount of cash, and we may not have sufficient cash or the ability to raise the funds necessary to settle conversions of the Notes in cash, repay the Notes at maturity or repurchase the Notes as required following a fundamental change.

On March 6, 2017, we issued $440.0 million aggregate principal amount of Notes.

Prior to December 1, 2021, the Notes are convertible at the option of the holders only under certain conditions or upon occurrence of certain events. Because the last reported sale price of our Class A common stock exceeded 130% of the applicable conversion price for the relevant period in the calendar quarter ending March 31, 2018, the Notes are convertible at the option of the holders thereof during the calendar quarter ending June 30, 2018. Whether the Notes will be convertible following such calendar quarter will depend on the continued satisfaction of this condition or another conversion conditions in the future. If holders of the Notes elect to convert their Notes, unless we elect to deliver solely shares of our Class A common stock to settle such conversion, we will be required to make cash payments in respect of the Notes being converted. In addition, holders of the Notes have the right to require us to repurchase all or a portion of their Notes upon the occurrence of a fundamental change (as defined in the indenture governing the Notes) at a repurchase price equal to 100% of the principal amount of the Notes to be repurchased, plus accrued and unpaid interest. If the Notes have not previously been converted or repurchased, we will be required to repay the Notes in cash at maturity.

Our ability to make required cash payments in connection with conversions of the Notes, repurchase the Notes in the event of a fundamental change or to repay or refinance the Notes at maturity will depend on market conditions and our future performance, which is subject to economic, financial, competitive and other factors beyond our control. We also may not use the cash proceeds we raised through the issuance of the Notes in an optimally productive and profitable manner. Since inception, our business has generated net losses and we may continue to incur significant losses. As a result, we may not have enough available cash or be able to obtain financing at the time we are required to repurchase or repay the Notes or pay cash with respect to Notes being converted.

In addition, our ability to repurchase or to pay cash upon conversion or at maturity of the Notes may be limited by law or regulatory authority. Our failure to repurchase Notes following a fundamental change or to pay cash upon conversion (unless we elect to deliver solely shares of our Class A common stock to settle such conversion) or at maturity of the Notes as required by the indenture would constitute a default under the indenture. A default under the indenture or the fundamental change itself could also lead to a default under our credit facility or agreements governing our future indebtedness and have a material adverse effect on our business, results of operations and financial condition. If the payment of the related indebtedness were to be accelerated after any applicable notice or grace periods, we may not have sufficient funds to repay the indebtedness and repurchase the Notes or to pay cash upon conversion or at maturity of the Notes.

Our reported financial results may be materially and adversely affected by changes in accounting principles generally accepted in the United States.

Generally accepted accounting principles in the United States are subject to interpretation by the Financial Accounting Standards Board (FASB), the SEC, and various bodies formed to promulgate and interpret appropriate accounting principles. A change in these principles or interpretations could have a significant effect on our reported financial results and could materially and adversely affect the transactions completed before the announcement of a change. Additionally, the adoption of new or revised accounting principles may require that we make significant changes to our systems, processes and controls.

For example, in February 2016, the FASB issued a new accounting standard for leasing which will be effective for us in fiscal year 2019. While we know it will have an impact, we are still evaluating the extent that this new accounting standard will impact our consolidated financial statements and related disclosures. Changes resulting from this and other new standards may result in materially different financial results and may require that we change how we process, analyze and report financial information and that we change financial reporting controls.

If currency exchange rates fluctuate substantially in the future, our financial results, which are reported in U.S. dollars, could be adversely affected.

As we continue to expand our global operations, we become more exposed to the effects of fluctuations in currency exchange rates. Our contracts are denominated primarily in U.S. dollars, and therefore the majority of our revenue are not subject to foreign currency risk. However, fluctuations in exchange rates of the U.S. dollar against foreign currencies could adversely affect our business, results of operations and financial condition. We incur expenses for employee compensation and other operating expenses at our non-U.S. locations in the local currency. Fluctuations in the exchange rates between the U.S. dollar and other currencies could result in the dollar equivalent of such expenses being higher. This could have a negative impact on our reported results of operations. From time to time, we may enter into forward contracts, options and/or foreign exchange swaps related to specific transaction exposures that arise in the normal course of our business, though we are not currently a party to any such hedging transactions. These and other such hedging activities may not eliminate our exposure to foreign exchange fluctuations. Moreover, the use of hedging instruments may introduce additional risks if we are unable to structure effective hedges with such instruments.

We may have exposure to greater-than-anticipated tax liabilities, which may materially and adversely affect our business.

We are subject to income taxes and non-income taxes in the United States and other countries in which we conduct business, and such laws and rates vary by jurisdiction. We are subject to review and audit by U.S. federal, state, local and foreign tax authorities. Such tax authorities may disagree with tax positions we take and if any such tax authority were to successfully challenge any such position, our financial results and operations could be materially and adversely affected. For example, the Office of the Treasurer and Tax Collector of the City and County of San Francisco (the "Tax Collector") has issued a decision regarding the Company's classification of its business activities. Although we disagree with the Tax Collector's decision and contest this classification, the ultimate resolution is uncertain and, if the Company does not prevail, we could have additional tax liabilities, which may adversely affect our financial condition and results of operations in the periods for which such determination is made. In addition, our future tax liability could be adversely affected by changes in tax laws, rates, and regulations. The determination of our worldwide provision for income and other taxes is highly complex and requires significant judgment, and there are many transactions and calculations where the ultimate tax determination is uncertain. Although we believe our estimates are reasonable, the amount ultimately payable may differ from amounts recorded in our financial statements and may materially affect our financial results in the period or periods for which such determination is made.

Federal income tax reform could have unforeseen effects on our financial condition and results of operations.

The 2017 Tax Cuts and Jobs Act ("2017 Tax Act") was enacted in December 2017 and contains many significant changes to U.S. Federal tax laws. The 2017 Tax Act requires complex computations that were not previously provided for under U.S. tax law. The Company has provided for an estimated effect of the 2017 Tax Act in its financial statements. The 2017 Tax Act requires significant judgments to be made in interpretation of the law and significant estimates in the calculation of the provision for income taxes. However, additional guidance may be issued by the IRS, Department of the Treasury, or other governing bodies that may significantly differ from the Company's interpretation of the law, which could have unforeseen effects on our financial condition and results of operations.

Risks Related to Ownership of Our Common Stock

The dual class structure of our common stock has the effect of concentrating voting control within our stockholders who held our stock prior to our initial public offering, including many of our employees and directors and their affiliates; this will limit or preclude your ability to influence corporate matters.

Our Class B common stock has ten votes per share, and our Class A common stock has one vote per share. Stockholders who hold shares of Class B common stock, including many of our executive officers, employees, and directors and their affiliates, held approximately 79.6% of the voting power of our combined outstanding capital stock as of March 31, 2018. Our executive officers and directors and their affiliates held approximately 75.2% of the voting power of our combined outstanding capital stock as of March 31, 2018. Because of the ten-to-one voting ratio between our Class B and Class A common stock, the holders of our Class B common stock collectively hold more than a majority of the combined voting power of our common stock, and therefore such holders are able to control all matters submitted to our stockholders for approval. When the shares of our Class B common stock represent less than 5% of the combined voting power of our Class A common stock and Class B common stock, the then-outstanding shares of Class B common stock will automatically convert into shares of Class A common stock.

Transfers by holders of Class B common stock will generally result in those shares converting to Class A common stock, subject to limited exceptions, such as certain transfers to entities, including certain charities and foundations, to the extent the transferor retains sole dispositive power and exclusive voting control with respect to the shares of Class B common stock. Such conversions of Class B common stock to Class A common stock upon transfer will have the effect, over time, of increasing the relative voting power of those holders of Class B common stock who retain their shares in the long term. If, for example, our Class B stockholders retain shares of Class B common stock constituting as little as 10% of all outstanding shares of our Class A and Class B common stock combined, they will continue to control a majority of the combined voting power of our outstanding capital stock.

We will continue to incur significantly increased costs and devote substantial management time as a result of operating as a public company.

As a public company, we incur significant legal, financial, and other expenses that we did not incur as a private company. We are subject to the reporting requirements of the Exchange Act and are required to comply with the applicable requirements of the Sarbanes-Oxley Act and the Dodd-Frank Wall Street Reform and Consumer Protection Act, as well as the rules and regulations subsequently implemented by the SEC and the listing standards of the New York Stock Exchange (NYSE), including changes in corporate governance practices and the establishment and maintenance of effective disclosure and financial controls. Continuing to comply with these requirements may increase our legal and financial compliance costs and may make some activities more time consuming and costly. In addition, our management and other personnel must divert attention from operational and other business matters to devote substantial time to these requirements. If we are unable to continue to meet these requirements, we may not be able to remain listed on the NYSE, which could result in potential loss of confidence by our customers and employees, loss of institutional investor interest, fewer business development opportunities, class action or shareholder derivative lawsuits, depressed stock price, limited liquidity of our Class A common stock, and other material adverse consequences. Moreover, we could incur additional compensation costs in the event that we decide to pay cash compensation closer to that of other public technology companies, which would increase our general and administrative expenses and could materially and adversely affect our profitability.

If we are unable to maintain effective disclosure controls and internal controls over financial reporting, investors may lose confidence in the accuracy and completeness of our financial reports, and the market price of our Class A common stock may be materially and adversely affected.

We are continuing to develop and refine our disclosure controls and improve our internal controls over financial reporting. We have expended, and anticipate that we will continue to expend, significant resources in order to maintain and improve the effectiveness of our disclosure controls and procedures and internal control over financial reporting.

Our current controls and any new controls that we develop may become inadequate because of changes in conditions in our business. Further, to the extent we acquire other businesses, the acquired company may not have a sufficiently robust system of internal controls and we may discover deficiencies. If we identify material weaknesses in our disclosure controls or internal control over financial reporting in the future, we will be unable to assert that our internal controls are effective. If we are unable to do so, or if our auditors are unable to attest to management’s report on the effectiveness of our internal controls, we could lose investor confidence in the accuracy and completeness of our financial reports, which could cause the price of our Class A common stock to decline. We have identified significant deficiencies in our internal control over financial reporting in the past and have taken steps to remediate such deficiencies. However, our efforts to remediate them may not be effective or prevent any future deficiency in our internal controls. We are required to disclose material changes made in our internal controls and procedures on a quarterly basis.

Any failure to maintain effective disclosure controls and internal control over financial reporting could have a material and adverse effect on our business and operating results, and cause a decline in the market price of our Class A common stock.

The market price of our Class A common stock has been and will likely continue to be volatile, and you could lose all or part of your investment.

The market price of our Class A common stock has been and may continue to be subject to wide fluctuations in response to various factors, some of which are beyond our control and may not be related to our operating performance. In addition to the factors discussed in this “Risk Factors” section and elsewhere in this Quarterly Report on Form 10-Q, factors that could cause fluctuations in the market price of our Class A common stock include the following:

- price and volume fluctuations in the overall stock market from time to time;
- volatility in the market prices and trading volumes of companies in our industry or companies that investors consider comparable;
- changes in operating performance and stock market valuations of other companies generally or of those in our industry in particular;
- sales of shares of our common stock by us or our stockholders;
- issuance of shares of our Class A common stock, whether in connection with an acquisition or upon conversion of some or all of our outstanding Notes;
- failure of securities analysts to maintain coverage and/or to provide accurate consensus results of us, changes in financial estimates by securities analysts who follow us, or our failure to meet these estimates or the expectations of investors;
- the financial or other projections we may provide to the public, any changes in those projections, or our failure to meet those projections;
- announcements by us or our competitors of new products or services;
- public reaction to our press releases, other public announcements, and filings with the SEC;
- rumors and market speculation involving us or other companies in our industry;
- actual or anticipated changes in our results of operations;

changes in the regulatory environment;

actual or anticipated developments in our business, our competitors' businesses, or the competitive landscape generally;
litigation involving us, our industry, or both, or investigations by regulators into our operations or those of our competitors;
announced or completed acquisitions of businesses or technologies by us or our competitors;
new laws or regulations or new interpretations of existing laws or regulations applicable to our business;
changes in accounting standards, policies, guidelines, interpretations, or principles;

actual or perceived data security incidents that we or our service providers may suffer;
any significant change in our management; and
general economic conditions and slow or negative growth of our markets.

In addition, in the past, following periods of volatility in the overall market and the market price of a particular company's securities, securities class action litigation has often been instituted against these companies. This litigation, if instituted against us, could result in substantial costs and a diversion of our management's attention and resources.

The convertible note hedge and warrant transactions may affect the value of our Class A common stock.

In connection with the issuance of the Notes, we entered into convertible note hedge transactions with certain financial institutions, which we refer to as the "option counterparties". We also entered into warrant transactions with the option counterparties pursuant to which we sold warrants for the purchase of our Class A common stock. The convertible note hedge transactions are expected generally to reduce the potential dilution to our Class A common stock upon any conversion of the Notes and/or offset any cash payments we are required to make in excess of the principal amount of converted Notes, as the case may be. The warrant transactions would separately have a dilutive effect to the extent that the market price per share of our Class A common stock exceeds the strike price of any warrants unless, subject to the terms of the warrant transactions, we elect to cash settle the warrants.
From time to time, the option counterparties or their respective affiliates may modify their hedge positions by entering into or unwinding various derivative transactions with respect to our Class A common stock and/or purchasing or selling our Class A common stock or other securities of ours in secondary market transactions prior to the maturity of the Notes. This activity could cause or avoid an increase or a decrease in the market price of our Class A common stock.

Anti-takeover provisions contained in our amended and restated certificate of incorporation, our amended and restated bylaws, and provisions of Delaware law, could impair a takeover attempt.

Our amended and restated certificate of incorporation, our amended and restated bylaws, and Delaware law contain provisions which could have the effect of rendering more difficult, delaying, or preventing an acquisition deemed undesirable by our board of directors and therefore depress the trading price of our Class A common stock.

Among other things, our amended and restated certificate of incorporation and amended and restated bylaws include provisions (i) creating a classified board of directors whose members serve staggered three-year terms; (ii) authorizing "blank check" preferred stock, which could be issued by our board of directors without stockholder approval and may contain voting, liquidation, dividend, and other rights superior to our common stock; (iii) limiting the ability of our stockholders to call special meetings; (iv) eliminating the ability of our stockholders to act by written consent without a meeting or to remove directors without cause; and (v) requiring advance notice of stockholder proposals for business to be conducted at meetings of our stockholders and for nominations of candidates for election to our board of directors. These provisions, alone or together, could delay or prevent hostile takeovers and changes in control or changes in our management.

As a Delaware corporation, we are also subject to provisions of Delaware law, including Section 203 of the Delaware General Corporation Law, which prevents certain stockholders holding more than 15% of our outstanding capital stock from engaging in certain business combinations without the approval of our board of directors or the holders of at least two-thirds of our outstanding capital stock not held by such stockholder.

Any provision of our amended and restated certificate of incorporation, amended and restated bylaws, or Delaware law that has the effect of delaying or preventing a change in control could limit the opportunity for our stockholders to receive a premium for their shares of our capital stock and could also affect the price that some investors are willing to pay for our Class A common stock.

Our amended and restated bylaws provide that the Court of Chancery of the State of Delaware will be the sole and exclusive forum for substantially all disputes between us and our stockholders, which could limit our stockholders' ability to obtain a favorable judicial forum for disputes with us or our directors, officers, or employees.

Our amended and restated bylaws provide that, unless we consent to the selection of an alternative forum, the Court of Chancery of the State of Delaware is the sole and exclusive forum for (i) any derivative action or proceeding brought on our behalf; (ii) any action asserting a claim of breach of fiduciary duty owed by any of our directors, officers, or other employees to us or to our stockholders; (iii) any action asserting a claim arising pursuant to the Delaware General Corporation Law; or (iv) any action asserting a claim governed by the internal affairs doctrine. The choice of forum provision may limit a stockholder's ability to bring a claim in a judicial forum that it finds favorable for disputes with us or our directors, officers, or other employees, which may discourage such lawsuits against us and our directors, officers, and other employees. Alternatively, if a court were to find the choice of forum provision contained in our amended and restated bylaws to be inapplicable or unenforceable in an action, we may incur additional costs associated with resolving such action in other jurisdictions, which could have a material and adverse impact on our business.

If securities or industry analysts publish reports that are interpreted negatively by the investment community, publish negative research reports about our business, or cease coverage of our company or fail to regularly publish reports on us, our share price and trading volume could decline.

The trading market for our Class A common stock depends, to some extent, on the research and reports that securities or industry analysts publish about us, our business, our market, or our competitors. We do not have any control over these analysts or the information contained in their reports. If one or more analysts publish research reports that are interpreted negatively by the investment community, or have a negative tone regarding our business, financial or operating performance, industry or end-markets, our share price could decline. In addition, if a majority of these analysts cease coverage of our company or fail to regularly publish reports on us, we could lose visibility in the financial markets, which could cause our share price or trading volume to decline.

We do not intend to pay dividends for the foreseeable future.

We currently intend to retain any future earnings to finance the operation and expansion of our business, and we do not expect to declare or pay any dividends in the foreseeable future. As a result, you may only receive a return on your investment in our common stock if the trading price of our common stock increases. Investors seeking cash dividends should not purchase shares of our common stock. Our ability to pay dividends is restricted by the terms of our revolving credit facility and is also subject to limitations imposed by certain financial regulations.

Additional stock issuances could result in significant dilution to our stockholders.

We may issue additional equity securities to raise capital, make acquisitions, or for a variety of other purposes. Additional issuances of our stock may be made pursuant to the exercise or conversion of new or existing convertible debt securities, warrants, stock options, or other equity incentive awards to new and existing service providers. Any such issuances will result in dilution to existing holders of our stock. We rely on equity-based compensation as an important tool in recruiting and retaining employees. The amount of dilution due to equity-based compensation of our employees and other additional issuances could be substantial.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds
Not applicable.

Item 3. Defaults Upon Senior Securities
Not applicable.

Item 4. Mine Safety Disclosures
Not applicable.

Item 5. Other Information
Not applicable.

Item 6. Exhibits
The documents listed in the Exhibit Index of this Quarterly Report on Form 10-Q are incorporated by reference or are filed with this Quarterly Report on Form 10-Q (numbered in accordance with Item 601 of Regulation S-K).

EXHIBIT INDEX

Exhibit Number	Description	Incorporated by Reference Form	File No.	Exhibit	Filing Date
31.1	Certification of Chief Executive Officer pursuant to Exchange Act Rules 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.				
31.2	Certification of Chief Financial Officer pursuant to Exchange Act Rules 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.				
32.1†	Certifications of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.				
101.INS	XBRL Instance Document.				
101.SCH	XBRL Taxonomy Extension Schema Document.				
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document.				
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document.				
101.LAB	XBRL Taxonomy Extension Labels Linkbase Document.				
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document.				

† The certifications attached as Exhibit 32.1 that accompany this Quarterly Report on Form 10-Q are deemed furnished and not filed with the Securities and Exchange Commission and are not to be incorporated by reference into any filing of Square, Inc. under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended, whether made before or after the date of this Quarterly Report on Form 10-Q, irrespective of any general incorporation language contained in such filing.

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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.

SQUARE, INC.

Date:	May 2, 2018	By:	/s/ Jack Dorsey
			Jack Dorsey
			President, Chief Executive Officer, and Chairman
			(Principal Executive Officer)
		By:	/s/ Sarah Friar
			Sarah Friar
			Chief Financial Officer
			(Principal Financial Officer)