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% Change
Transaction revenue
$
300,453

$
211,110

$
89,343

42
%
Starbucks transaction revenue
38,838

29,237

$
9,601

33
%
Software and data product revenue
23,796

8,006

$
15,790

197
%
Hardware revenue
16,182

2,204

$
13,978

634
%
Total net revenue
$
379,269

$
250,557

$
128,712

51
%
Total net revenue for the three months ended March 31, 2016, increased by $128.7 million, or 51%, compared to the three months ended March 31, 2015.
Transaction revenue for the three months ended March 31, 2016, increased by $89.3 million, or 42%, compared to the three months ended March 31, 2015. This increase was attributable to growth in GPV processed of $3.2 billion, or 45%, to $10.3 billion from $7.1 billion. The majority of GPV growth was derived from new sellers added within the three months ended March 31, 2016; a smaller portion was generated by GPV growth from the payment activity of existing sellers that were approved to transact with us on or prior to March 31, 2015. Transaction revenue contributed 79% of total net revenue in the three months ended March 31, 2016, compared to 84% in the three months ended March 31, 2015.
Starbucks transaction revenue for the three months ended March 31, 2016, increased by $9.6 million, or 33%, compared to the three months ended March 31, 2015. Starbucks transaction revenue contributed 10% of total net revenue in the three months ended March 31, 2016, compared to 12% in the three months ended March 31, 2015. Under our amended payment processing agreement effective October 1, 2015, Starbucks agreed to pay increased processing rates to us for as long as it continues to process transactions with us. While Starbucks announced that it would transition to another payment processor prior to the expiration of the payment processing agreement in the third quarter of 2016, we continued to process a portion of Starbucks payments, generating transaction revenue at the newly increased rates.
Software and data product revenue for the three months ended March 31, 2016, increased by $15.8 million, or 197%, compared to the three months ended March 31, 2015. The increase was driven by the launch and expansion of new products and services in 2015 and 2016, including instant deposits. During the three months ended March 31, 2016, Square Capital and Caviar remained the largest contributors to software and data product revenue. Software and data product revenue contributed 6% of total net revenue in the three months ended March 31, 2016, compared to 3% in the three months ended March 31, 2015.
Hardware revenue for the three months ended March 31, 2016, increased by $14.0 million, or 634%, compared to the three months ended March 31, 2015. The increase primarily reflects growth in shipments of our Square Reader for Europay,

24

MasterCard, and Visa (EMV) chip cards and near field communication (NFC) following its launch in the fourth quarter of 2015. We also continued to generate increased sales of Square Stand and third-party peripherals. Hardware revenue contributed 4% of total net revenue in the three months ended March 31, 2016, compared to 1% in the three months ended March 31, 2015.

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

	Three Months Ended March 31,			
	2016	2015	$ Change	% Change
Transaction costs	$194,276	$132,107	$62,169	47 %
Starbucks transaction costs	36,610	36,211	$399	1 %
Software and data product costs	9,033	3,155	$5,878	186 %
Hardware costs	26,740	4,197	$22,543	537 %
Amortization of acquired technology	2,370	602	$1,768	294 %
Total cost of revenue	$269,029	$176,272	$92,757	53 %

Total cost of revenue for the three months ended March 31, 2016, increased by $92.8 million, or 53%, compared to the three months ended March 31, 2015.

Transaction costs for the three months ended March 31, 2016, increased by $62.2 million, or 47%, compared to the three months ended March 31, 2015. This increase was primarily attributable to growth in GPV processed of $3.2 billion, or 45%, compared to the three months ended March 31, 2015.

Starbucks transaction costs for the three months ended March 31, 2016, increased by $0.4 million, or 1%, compared to the three months ended March 31, 2015. As a result of Starbucks' agreement to pay us increased processing rates effective October 1, 2015, growth in Starbucks transaction revenue outpaced growth in Starbucks transaction costs compared to the prior year period.

Software and data product costs for the three months ended March 31, 2016, increased by $5.9 million, or 186%, compared to the three months ended March 31, 2015, primarily reflecting increased costs associated with growth and expansion of Caviar. To a lesser extent we also incurred increased amortization costs related to the development of certain software and data products.

Hardware costs for the three months ended March 31, 2016, increased by $22.5 million, or 537%, compared to the three months ended March 31, 2015. The increase primarily reflects growth in shipments of our Square Reader for EMV chip cards and NFC following its launch in the fourth quarter of 2015, and to a lesser extent, increased sales of Square Stand and third-party peripherals. Hardware costs associated with the production of Square Stand exceed the revenue we derive from sales of Square Stand. For the three months ended March 31, 2016, hardware costs grew more slowly than hardware revenue as a result of increased sales of third-party peripherals and the introduction of our Square Reader for EMV chip cards and NFC.

Amortization of acquired technology for the three months ended March 31, 2016, increased by $1.8 million, or 294%, compared to the three months ended March 31, 2015. The increase was related to new technology assets obtained through acquisitions that occurred in 2015.

Operating Expenses (in thousands, except for percentages)

	Three Months Ended March 31,			
	2016	2015	$ Change	% Change
Product development	$64,592	$39,545	$25,047	63 %
% of total net revenue	17 %	16 %		
Sales and marketing	$38,496	$36,181	$2,315	6 %
% of total net revenue	10 %	14 %		
General and administrative	$96,107	$28,119	$67,988	242 %
% of total net revenue	25 %	11 %		
Transaction and advance losses	$7,861	$16,322	$(8,461)	(52)%
% of total net revenue	2 %	7 %		
Amortization of acquired customer assets	$317	$468	$(151)	(32)%
% of total net revenue	— %	— %		
Total operating expenses	$207,373	$120,635	$86,738	72 %

Product development expenses for the three months ended March 31, 2016, increased by $25.0 million, or 63%, compared to the three months ended March 31, 2015, primarily due to an increase in engineering, design, and product personnel in the period from March 31, 2015 to March 31, 2016, and increased tooling costs associated with the development of our next generation hardware products. For the three months ended March 31, 2016, product development expenses included $21.9 million of share-based compensation expense, representing a $13.0 million increase compared to the three months ended March 31, 2015. For the three months ended March 31, 2016, product development expenses also included $3.1 million of depreciation expense, representing a $0.3 million increase compared to the three months ended March 31, 2015.

Sales and marketing expenses for the three months ended March 31, 2016, increased by $2.3 million, or 6%, compared to the three months ended March 31, 2015, primarily due to an increase in sales and marketing personnel in the period from March 31, 2015 to March 31, 2016, and increased costs associated with our Square Cash peer-to-peer transfer service. This increase was offset in part by a decrease of $2.4 million in paid marketing expenses primarily due to elevated TV advertising in the prior year period. For the three months ended March 31, 2016, sales and marketing expenses included $2.9 million of share-based compensation expense, representing a $1.5 million increase compared to the three months ended March 31, 2015.

General and administrative expenses for the three months ended March 31, 2016, increased by $68.0 million, or 242%, compared to the three months ended March 31, 2015, due in large part to an increase in customer support, legal, compliance, and finance personnel in the period from March 31, 2015 to March 31, 2016. For the three months ended March 31, 2016, general and administrative expenses included $50.0 million of expense related to a litigation accrual, with no similar activity during the three months ended March 31, 2015. This accrual represents an estimate of potential losses related to ongoing legal proceedings with Robert E. Morley. The balance of the increased expenses in the period was primarily due to increased third-party legal, finance, consulting and certain software license expenses. For the three months ended March 31, 2016, general and administrative expenses included $6.3 million of share-based compensation expense, representing a $3.3 million increase compared to the three months ended March 31, 2015.

Transaction and advance losses for the three months ended March 31, 2016, decreased by $8.5 million compared to the three months ended March 31, 2015. During the three months ended March 31, 2015, we accrued an estimate of $5.7 million related to a fraud loss from a single seller, with no similar activity during the three months ended March 31, 2016. The remaining decrease is primarily a result of an update to our provision estimates for Square Capital, which we continue to refine as more historical data becomes available.

Amortization of acquired customer assets for the three months ended March 31, 2016, decreased by $0.2 million compared to the three months ended March 31, 2015, primarily as a result of certain customer assets reaching end of life.

26

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

	Three Months Ended March 31,			
	2016	2015	$ Change	% Change
Interest (income) and expense, net	$69	$414	$(345)	(83)%
Other (income) and expense, net	(786)	796	$(1,582)	(199)%

Interest (income) and expense, net, for the three months ended March 31, 2016, decreased by $0.3 million compared to the three months ended March 31, 2015, primarily driven by interest income earned on our recent investment in marketable securities offsetting most of our interest expense.

Other (income) and expense, net, for the three months ended March 31, 2016, changed by $1.6 million compared to the three months ended March 31, 2015, driven primarily by favorable fluctuations in foreign exchange rates.

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

	Three Months Ended March 31,			
	2016	2015	$ Change	% Change
Provision for income taxes	$339	$418	$ (79)	(19)%
Effective tax rate	(0.4)%	(0.9)%		

Provision for income taxes for the three months ended March 31, 2016, decreased by $0.1 million compared to the three months ended March 31, 2015.

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 revenue, net (loss) income, and other results under generally accepted accounting principles in the United States (GAAP), the following table sets forth key operating metrics and non-GAAP financial measures we use to evaluate our business. Each of these metrics and measures excludes the effect of our payment processing agreement with Starbucks. We do not intend to renew our payment processing agreement with Starbucks when it expires in the third quarter of 2016, and we amended the agreement to eliminate the exclusivity provision in order to permit Starbucks to begin transitioning to another payment processor starting October 1, 2015. Under the amendment, Starbucks also agreed to pay increased processing rates to us for as long as it continues to process transactions with us. Starbucks has announced that it will transition to another payment processor and will cease using our payment processing services altogether prior to the scheduled expiration of the agreement in the third quarter of 2016. As a result, we believe it is useful to exclude Starbucks activity to clearly show the impact Starbucks has had on our financial results historically, to provide insight into the impact of the expected termination of the Starbucks agreement on our revenues going forward, to facilitate period-to-period comparisons of our business, and to facilitate comparisons of our performance to that of other payment processors. Our agreements with other sellers, including Starbucks following the amendment described above, generally provide both those sellers and us the unilateral right to terminate such agreements at any time, without fine or penalty. Furthermore, we generally do not enter into long-term contractual agreements with sellers.

	Three Months Ended March 31,			
	2016	2015	$ Change	% Change
	(in thousands, except GPV)			

Gross Payment Volume (GPV) (in millions)	$10,290	$7,117	$3,174	45 %
Adjusted Revenue	$146,155	$89,213	$56,942	64 %
Adjusted EBITDA	$(9,083)	$(20,129)	$11,046	NM

27

Gross Payment Volume (GPV)
We define GPV as the total dollar amount of all card payments processed by sellers using Square, net of refunds. GPV excludes card payments processed for Starbucks. Additionally, GPV excludes activity related to our Square Cash peer-to-peer payments service.

Adjusted Revenue
Adjusted Revenue is a non-GAAP financial measure that we define as our total net revenue less transaction costs, adjusted to eliminate the effect of activity under our payment processing agreement with Starbucks. As described above, Starbucks has announced that it will transition to another payment processor and will cease using our payment processing services altogether, and we believe that providing Adjusted Revenue metrics that exclude the impact of our agreement with Starbucks is useful to investors.
We believe it is useful to exclude transaction costs from Adjusted Revenue as this is a primary metric used by management to measure our business performance, and it affords greater comparability to other payment processing companies. Substantially all of the transaction costs excluded from Adjusted Revenue are interchange fees set by payment card networks and are paid to card issuers, with the remainder of such transaction costs consisting of assessment fees paid to payment card networks, fees paid to third-party payment processors, and bank settlement fees. While some payment processors present their revenue in a similar fashion to us, others present their revenue net of transaction costs because they pass through these costs directly to their sellers. Under our standard pricing model, we do not pass through these costs directly to our sellers.
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 excludes transaction costs, which is our largest cost of revenue item; and
- other companies, including companies in our industry, may calculate Adjusted Revenue differently from how we calculate this measure 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,			
	2016	2015	$ Change	% Change
	(in thousands)			
Total net revenue	$379,269	$250,557	$128,712	51 %
Less: Starbucks transaction revenue	38,838	29,237	9,601	33 %
Less: transaction costs	194,276	132,107	62,169	47 %
Adjusted Revenue	$146,155	$89,213	$56,942	64 %

Adjusted EBITDA
Adjusted EBITDA is a non-GAAP financial measure that represents our net loss, adjusted to eliminate the effect of Starbucks transaction revenue, Starbucks transaction costs and a litigation accrual described in Note 17 of the Notes to the Condensed Consolidated Financial Statements, before interest income and expense, provision or benefit for income taxes, depreciation, amortization, share-based compensation expense, other income and expense, the gain or loss on the sale of property and equipment and impairment of intangible assets. We have included Adjusted EBITDA in this Quarterly Report on Form 10-Q because it is a key measure 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 that Adjusted EBITDA provides 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, it provides a useful measure for period-to-period comparisons of our business, as it removes the effect of certain non-cash items and certain variable charges.

We believe it is useful to exclude non-cash charges, such as depreciation and amortization, and share-based compensation expenses, from our Adjusted EBITDA because the amount of such expenses in any specific period may not directly correlate to the underlying performance of our business operations. We exclude Starbucks transaction revenue and Starbucks transaction costs because Starbucks has announced that it will transition to another payment processor prior to the scheduled expiration of our payment processing agreement in the third quarter of 2016. We believe that providing Adjusted EBITDA metrics that exclude the impact of our agreement with Starbucks is useful to investors. We exclude the litigation accrual described in Note 17 of the Notes to the Condensed Consolidated Financial Statements, gain or loss on the sale of property and equipment and impairment of intangible assets from Adjusted EBITDA because we do not believe that these items are reflective of our ongoing business operations. In addition, we believe it is useful to exclude 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. Adjusted EBITDA 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:

- although depreciation and amortization are non-cash charges, the assets being depreciated and amortized may have to be replaced in the future, and Adjusted EBITDA does not reflect cash capital expenditure requirements for such replacements or for new capital expenditures or other capital commitments;

- Adjusted EBITDA does not reflect changes in, or cash requirements for, our working capital needs;

- Adjusted EBITDA does not reflect the effect of income taxes that may represent a reduction in cash available to us;

- Adjusted EBITDA does not reflect the effect of foreign currency exchange gains or losses which is included in other income and expense; and

- other companies, including companies in our industry, may calculate Adjusted EBITDA differently from how we calculate this measure or not at all, which reduces its usefulness as a comparative measure.

Because of these limitations, you should consider Adjusted EBITDA 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:

	Three Months Ended March 31,			
	2016	2015	$ Change	% Change
	(in thousands)			
Net loss	$(96,755)	$(47,978)	$(48,777)	NM
Starbucks transaction revenue	(38,838)	(29,237)	(9,601)	NM
Starbucks transaction costs	36,610	36,211	399	1 %
Share-based compensation expense	31,198	13,461	17,737	132 %
Depreciation and amortization	9,118	5,546	3,572	64 %
Litigation accrual	50,000	—	50,000	— %
Interest (income) and expense	69	414	(345)	(83)%
Other (income) and expense	(786)	796	(1,582)	(199)%
Provision for income taxes	339	418	(79)	(19)%
Loss (gain) on sale of property and equipment	(38)	240	(278)	(116)%
Adjusted EBITDA	$(9,083)	$(20,129)	$11,046	NM

29

Liquidity and Capital Resources

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

	March 31, 2016	December 31, 2015
Cash and cash equivalents	$370,646	$ 470,775
Short-term investments	$43,447	$ —
Long-term investments	$29,715	$ —
Short-term restricted cash	$13,542	$ 13,537
Long-term restricted cash	$14,994	$ 14,686

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

	Three Months Ended March 31,	
	2016	2015
Net cash used in operating activities	$(15,511)	$(10,950)
Net cash used in investing activities	$(81,326)	$(14,269)
Net cash (used in) provided by financing activities	$(4,850)	$1,749
Effect of foreign exchange rate changes on cash and cash equivalents	$1,558	$(860)
Net decrease in cash and cash equivalents	$(100,129)	$(24,330)

Our principal sources of liquidity are our cash, cash equivalents and investments in marketable securities. As of March 31, 2016, we had $443.8 million of cash, 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. In November 2015, we completed our initial public offering in which we received total net proceeds of $245.7 million after deducting underwriting discounts and commissions of $14.7 million and other offering expenses of $6.9 million. Prior to our initial public offering, our principal source of liquidity was private sales of convertible preferred stock with total cash proceeds to us of $544.9 million.

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 paid $0.1 million in unused commitment fees during the three months ended March 31, 2016.

We fund a majority of our MCAs from arrangements with third parties that commit to purchase the future receivables related to these advances. In addition to MCAs, we are expanding Square Capital further to offer new types of services, including merchant loans. We believe that our existing cash and cash equivalents and availability under our line of credit will be sufficient to meet our working capital needs 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 be assured that any additional financing will be available to us on acceptable terms or at all.

Short-term restricted cash of $13.5 million as of March 31, 2016, reflects pledged cash deposited into savings accounts at the financial institutions that process our sellers' payments transactions. 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

30

of these payments. We have recorded this amount as a current asset on our condensed 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.
Long-term restricted cash of $15.0 million as of March 31, 2016, 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. We have recorded this amount as a non-current asset on the condensed consolidated balance sheets as the terms of the related leases extend beyond one year.

We experience significant day-to-day fluctuations in our cash and cash equivalents, 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, settlement receivable and customer 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, settlement receivable and customer payable amounts increase. Typically our cash, cash equivalents, settlement receivable and customer payable balances at period end represent one to four days of receivables and disbursements to be made in the subsequent period. Customer payable and settlement receivable balances typically move in tandem, as pay-out and pay-in largely occur on the same business day. However, customer payable balances will be greater in amount than settlement receivable 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 used in operating activities consisted of net loss adjusted for certain non-cash items including depreciation and amortization, share-based compensation expense, provisions for transaction losses, excess tax benefit from share based award activity, provision for uncollectible seller cash advances, deferred income taxes and impairment of intangible assets, as well as the effect of changes in operating assets and liabilities, including working capital.
For the three months ended March 31, 2016, cash used by operating activities was $15.5 million, as a result of a net loss of $96.8 million, offset by non-cash items consisting of share-based compensation of $31.2 million, depreciation and amortization of $9.1 million, and provision for transaction losses of $7.2 million. Additional uses of cash were from changes in operating assets and liabilities, including increases in settlements receivable of $46.5 million, other current assets of $13.3 million, and merchant cash advance receivables of $11.8 million, offset in part by increases in customers payable of $58.9 million and accrued expenses of $55.8 million.
For the three months ended March 31, 2015, cash used by operating activities was $11.0 million, as a result of a net loss of $48.0 million, offset in part by non-cash items consisting of share-based compensation expense of $13.5 million, provision for transaction losses of $13.8 million and depreciation and amortization of $5.5 million. Additional uses of cash were from changes in our operating assets and liabilities, including an increase in settlements receivable of $34.0 million, offset by an increase in customers payable of $38.6 million.

Cash Flows from Investing Activities
Cash flows used in investing activities primarily relate to capital expenditures to support our growth, changes in restricted cash, and business acquisitions.
For the three months ended March 31, 2016, cash used in investing activities was $81.3 million as a result of the purchase of marketable securities of $73.1 million and the purchase of property and equipment of $7.5 million.
For the three months ended March 31, 2015, cash used in investing activities was $14.3 million as a result of the purchase of property and equipment of $10.4 million and business acquisitions of $3.8 million.

Cash Flows from Financing Activities

31

For the three months ended March 31, 2016, cash used in financing activities was $4.9 million as a result of payments in offering costs related to our initial public offering, offset in part by proceeds from the exercise of stock options. For the three months ended March 31, 2015, cash provided by financing activities was $1.7 million as a result of proceeds from the exercise of stock options.

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, 2015.

Off-Balance Sheet Arrangements

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

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, 2015.

Our critical accounting policies have not materially changed during the three months ended March 31, 2016. 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 the assumptions and estimates associated with revenue recognition, accrued transaction losses, provision for uncollectible receivables related to MCAs, business combinations, goodwill and intangible assets, income taxes, and share-based compensation to have the greatest potential effect on our consolidated financial statements. Therefore, we consider these to be our critical accounting policies and estimates.

Recent Accounting Pronouncements

See “Recently Issued Accounting Standards” in Note 1 of the accompanying notes to our 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, 2016, 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 and the intent to hold these instruments until maturity which further reduces 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 10% 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, and Australian Dollar. 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

As of the end of the period covered by this Quarterly Report on Form 10-Q, our management, with the participation of the Chief Executive Officer and Chief Financial Officer, performed an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures as defined in Rule 13a-15(e) promulgated under the Securities Exchange Act of 1934, as amended (the Exchange Act). Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that as of March 31, 2016, our disclosure controls and procedures were effective to provide reasonable assurance that information required to be disclosed in our reports filed or submitted under the Exchange Act were recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission’s rules and forms, and that information required to be disclosed by us in the reports we file under the Exchange Act (according to Rule 13(a)-15(e)) is accumulated and communicated to our management, including the Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

Changes in Internal Control over Financial Reporting

There was no change in our internal control over financial reporting identified in connection with the evaluation required by Rule 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. Notably, we are currently involved in ongoing legal proceedings with Robert E. Morley and REM Holdings 3, LLC (REM). In two related proceedings, we are litigating disputes over certain patents and over Mr. Morley’s early involvement in the business enterprise that became Square.

On December 1, 2010, we, along with our co-founder Jim McKelvey, filed a complaint (2010 Complaint) in the United States District Court for the Eastern District of Missouri (District Court), which, as amended, concerns the inventorship, ownership, implied license, non-infringement, invalidity, and unenforceability of three patents: U.S. Patent Nos. 7,918,394 (‘394 Patent), 7,810,729 (‘729 Patent), and 7,896,248 (‘248 Patent). All three patents are in a single patent family directed to card reader technology. The patents, which the U.S. Patent and Trademark Office (PTO) granted in 2010 and 2011, name Mr. Morley as the sole inventor and REM as their assignee of rights. The 2010 Complaint sought to add Mr. McKelvey as a named inventor of those patents given his significant contributions to the claimed inventions. REM counterclaimed, alleging infringement by Square of the three patents, and we subsequently requested that the PTO reexamine those patents.

On January 17, 2012, the PTO issued a reexamination certificate invalidating the entirety of the ‘394 Patent. With the ‘394 Patent invalidated, two patents remained for consideration by the PTO: the ‘729 Patent and the ‘248 Patent. In April 2012, the PTO reexamination examiner closed prosecution on those two patents, rejecting all of the claims of the ‘729 Patent and 13 of the 20 claims of the ‘248 Patent as invalid in view of prior art. REM appealed the reexamination examiner’s rejections on these two remaining patents to the Patent Office Trial and Appeals Board (PTAB), and we appealed to have the PTAB reject the remaining seven claims of the ‘248 Patent and to recognize additional grounds for rejection of the previously rejected ‘248 Patent and ‘729 Patent claims. In March 2014, the PTAB issued a decision in our favor, affirming the rejection of all claims of the ‘729 Patent, affirming the rejection of the 13 claims of the ‘248 Patent, and ruling that the reexamination examiner should also reject the remaining seven claims of the ‘248 Patent (having so ruled, the PTAB did not need to consider additional grounds for rejecting the ‘248 and ‘729 Patent claims). Following the PTAB’s ruling, REM filed a response on the ‘248 Patent, substantially amending (i.e., adding new limitations to) five of the seven claims the PTAB had found to be unpatentable. On June 5, 2015, the PTO reexamination examiner, having considered the newly amended claims on remand, issued a preliminary determination that the new limitations allowed those five dependent claims to overcome the grounds for the PTAB’s rejection ruling. The PTO reexamination examiner noted, however, that at least four of the five new claims were still unpatentable because they were indefinite, impermissibly broad, or lacked support in the specification. Additionally, on September 8, 2015, REM filed a notice of appeal at the Court of Appeals for the Federal Circuit challenging the PTAB’s decision regarding the ‘729 Patent. Our arguments with respect to the remaining claims of the ‘248 Patent at the PTAB and the appeal by REM with respect to the ‘729 Patent are still pending, and we intend to pursue them vigorously. With the exception of these five more recently amended claims, which have not yet progressed beyond preliminary reexamination examiner review, all of the claims from all three patents asserted in the 2010 Complaint have either been canceled or otherwise found unpatentable by the PTAB.

On January 30, 2014, three weeks after the PTAB hearing that resulted in the rejection of all of Mr. Morley’s and REM’s remaining claims of the patents in the 2010 Complaint, Mr. Morley and REM filed a complaint against us and against Jack Dorsey and Mr. McKelvey, in the District Court, alleging that the formation of Square and the development of our card reader and decoding technologies constituted, among other things, breach of an alleged joint venture, fraud, negligent misrepresentation, civil conspiracy, unjust enrichment, and misappropriation of trade secrets, as well as other related claims (2014 Complaint). Mr. Morley contends as part of his alleged joint venture claim, among others, that he was an equal partner with Mr. Dorsey and Mr. McKelvey in the business enterprise that ultimately evolved into Square, and that Mr. Dorsey and Mr. McKelvey breached their alleged joint venture agreement with Mr. Morley by excluding him from ownership in Square. Mr. Morley claims that to the extent the defendants contend that no joint venture was formed, Mr. McKelvey and Mr. Dorsey committed fraud, negligent misrepresentation, and/or fraudulent nondisclosure. The 2014 Complaint also alleges infringement of another patent related to the ‘248, ‘394, and ‘729 Patents, U.S. Patent No. 8,584,946 (‘946 Patent). Mr. Morley is seeking a judgment and order that Square, Mr. Dorsey, and Mr. McKelvey hold ownership of Square in constructive trust for Mr. Morley, as well as a variety of additional damages, injunctive relief, royalties, and correction of inventorship of certain of our patents.

Even prior to the filing of the 2014 Complaint, on December 31, 2013, we had filed a petition at the PTAB requesting inter partes review (IPR) proceedings to invalidate the ‘946 Patent. On July 7, 2015, the PTAB issued a decision on the IPR, rejecting 12 of the 17 claims of the ‘946 patent, including all independent claims, to be invalid based on prior art. On November 20, 2015, the PTAB rejected two additional claims of the ‘946 patent in response to our request for rehearing. Consequently, 14

35

of the 17 claims of the ‘946 patent stand rejected. On February 9, 2016, we filed an ex parte reexamination request at the patent office to invalidate the three remaining claims of the ‘946 patent. On March 30, 2016, the patent office granted our request and instituted reexamination on all three claims.

We moved to consolidate the 2014 Complaint with the 2010 Complaint (the Complaints), and the District Court granted our motion on July 16, 2014. We moved to dismiss certain claims as time barred under California and Delaware law, and the District Court denied the motion on October 16, 2014, applying Missouri law. We moved to stay counts of the 2014 Complaint related to alleged infringement of the ‘946 Patent and inventorship of certain of our patents, pending the ongoing PTO proceedings, and on April 2, 2015, the District Court granted our motion to stay. The District Court has issued a scheduling order that sets forth the current expected schedule of important events in the proceedings, but no assurances can be given that the schedule will not change. A two-week trial is currently scheduled for June 13, 2016. We are vigorously defending against the Complaints. Notably, we filed a Motion for Summary Judgment on January 20, 2016. On April 22, 2016, the District Court denied our Motion for Summary Judgment. We recently signed a binding term sheet with Mr. Morley and REM stipulating the material terms of a settlement. While the final definitive agreement has not yet been finalized, we have recorded a charge of $50.0 million in general and administrative expenses for three months ended March 31, 2016. Until we enter into a final definitive agreement, we can make no assurances about the specific settlement terms, including monetary and nonmonetary terms.

Additionally, we are 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 Northern District of California against our wholly owned subsidiary, Caviar, Inc., which, as amended, alleges 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. Mr. Levin also sought an award of penalties pursuant to the Labor Code Private Attorneys General Act of 2004 on behalf of the putative class. On March 29, 2016, the Court entered a Notice of Intent to Dismiss the lawsuit, and on May 2, 2016, the Court dismissed the lawsuit in its entirety. The parties stipulated that certain dismissed claims may be pursued by a different courier, if plaintiff's counsel so chooses.

In addition, from time to time, we are involved in various other litigation matters and disputes arising in the ordinary course of business. While it is not feasible to predict or determine the ultimate outcome of these matters, we believe that none of our current legal proceedings will have a material adverse effect on our business.

Item 1A. Risk Factors

The risks described in Item 1A, “Risk Factors,” contained in our Annual Report on Form 10-K for the year ended December 31, 2015, could materially and adversely affect our business, financial condition, and results of operations. There have been no material changes in such risks during the three months ended March 31, 2016.

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.

36

Item 6. Exhibits

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

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 6, 2016	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 Accounting and Financial Officer)

EXHIBIT INDEX

Exhibit Number	Description
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.