

CHIPOTLE MEXICAN GRILL INC

Form 10-Q

October 25, 2017

Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2017

or

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from            to

Commission File Number: 1-32731

CHIPOTLE MEXICAN GRILL, INC.

(Exact name of registrant as specified in its charter)

Delaware  
(State or other jurisdiction of  
incorporation or organization)

84-1219301  
(IRS Employer  
Identification No.)

Edgar Filing: CHIPOTLE MEXICAN GRILL INC - Form 10-Q

1401 Wynkoop St., Suite 500 Denver, CO 80202  
(Address of Principal Executive Offices) (Zip Code)

Registrant's telephone number, including area code: (303) 595-4000

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See definitions of "large accelerated filer," "accelerated filer," "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Accelerated filer

Non-accelerated filer

(Do not check if a smaller reporting company) Smaller reporting company

Emerging growth company

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

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

As of October 20, 2017, there were 28,232,923 shares of the registrant's common stock, par value of \$0.01 per share outstanding.

Table of Contents

TABLE OF CONTENTS

|          |  |    |
|----------|--|----|
| PART I   |  |    |
| Item 1.  | <u>Financial Statements</u>  | 1  |
| Item 2.  | <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u> | 10 |
| Item 3.  | <u>Quantitative and Qualitative Disclosures About Market Risk</u>                            | 14 |
| Item 4.  | <u>Controls and Procedures</u>   | 15 |
| PART II  |  |    |
| Item 1.  | <u>Legal Proceedings</u>   | 15 |
| Item 1A. | <u>Risk Factors</u>  | 15 |
| Item 2.  | <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>                           | 16 |
| Item 3.  | <u>Defaults Upon Senior Securities</u>   | 16 |
| Item 4.  | <u>Mine Safety Disclosures</u>   | 16 |
| Item 5.  | <u>Other Information</u>   | 16 |
| Item 6.  | <u>Exhibits</u>  | 17 |
|          | <u>Signatures</u>  | 18 |

---

Table of Contents

## PART I

## ITEM 1. FINANCIAL STATEMENTS

Chipotle Mexican Grill, Inc.

Condensed Consolidated Balance Sheet

(in thousands, except per share data)

|  | September<br>30,<br>2017<br>(unaudited) | December 31,<br>2016 |
|--|---|----------------------|
| Assets   |   |                      |
| Current assets:  |   |                      |
| Cash and cash equivalents  | \$ 113,480                              | \$ 87,880            |
| Accounts receivable, net of allowance for doubtful accounts of \$39 and \$259 as of September 30, 2017 and December 31, 2016, respectively                 | 23,870                                  | 40,451               |
| Inventory  | 21,634                                  | 15,019               |
| Prepaid expenses and other current assets  | 49,089                                  | 44,080               |
| Income tax receivable  | 12,986                                  | 5,108                |
| Investments  | 434,877                                 | 329,836              |
| Total current assets   | 655,936                                 | 522,374              |
| Leasehold improvements, property and equipment, net  | 1,331,786                               | 1,303,558            |
| Long term investments  | -                                       | 125,055              |
| Other assets   | 54,716                                  | 53,177               |
| Goodwill   | 21,939                                  | 21,939               |
| Total assets   | \$ 2,064,377                            | \$ 2,026,103         |
| Liabilities and shareholders' equity   |   |                      |
| Current liabilities:   |   |                      |
| Accounts payable   | \$ 86,705                               | \$ 78,363            |
| Accrued payroll and benefits   | 108,120                                 | 76,301               |
| Accrued liabilities  | 128,577                                 | 127,129              |
| Total current liabilities  | 323,402                                 | 281,793              |
| Deferred rent  | 309,446                                 | 288,927              |
| Deferred income tax liability  | 7,577                                   | 18,944               |
| Other liabilities  | 36,826                                  | 33,946               |
| Total liabilities  | 677,251                                 | 623,610              |
| Shareholders' equity:  |   |                      |
| Preferred stock, \$0.01 par value, 600,000 shares authorized, no shares issued as of September 30, 2017 and December 31, 2016, respectively                | -                                       | -                    |
| Common stock \$0.01 par value, 230,000 shares authorized, and 35,851 and 35,833 shares issued as of September 30, 2017 and December 31, 2016, respectively | 359                                     | 358                  |
| Additional paid-in capital   | 1,294,315                               | 1,238,875            |
| Treasury stock, at cost, 7,564 and 7,019 common shares at September 30, 2017 and December 31, 2016, respectively   | (2,257,174)                             | (2,049,389)          |

Edgar Filing: CHIPOTLE MEXICAN GRILL INC - Form 10-Q

|   |              |              |
|---|--------------|--------------|
| Accumulated other comprehensive income (loss) | (3,645)      | (8,162)      |
| Retained earnings                             | 2,353,271    | 2,220,811    |
| Total shareholders' equity                    | 1,387,126    | 1,402,493    |
| Total liabilities and shareholders' equity    | \$ 2,064,377 | \$ 2,026,103 |

See accompanying notes to condensed consolidated financial statements.

1

---

Table of Contents

Chipotle Mexican Grill, Inc.

Condensed Consolidated Statement of Income

(unaudited)

(in thousands, except per share data)

|   | Three months ended<br>September 30, |              | Nine months ended<br>September 30, |              |
|---|-------------------------------------|--------------|------------------------------------|--------------|
|   | 2017                                | 2016         | 2017                               | 2016         |
| Revenue   | \$ 1,128,074                        | \$ 1,036,982 | \$ 3,366,312                       | \$ 2,869,824 |
| Restaurant operating costs (exclusive of depreciation and amortization shown separately below): |                                     |              |                                    |              |
| Food, beverage and packaging  | 394,567                             | 363,900      | 1,155,514                          | 999,968      |
| Labor   | 306,862                             | 286,144      | 900,564                            | 820,751      |
| Occupancy   | 83,199                              | 74,201       | 242,482                            | 217,147      |
| Other operating costs   | 162,312                             | 166,045      | 476,606                            | 473,390      |
| General and administrative expenses   | 99,182                              | 78,405       | 238,698                            | 211,171      |
| Depreciation and amortization   | 41,546                              | 37,434       | 121,906                            | 108,296      |
| Pre-opening costs   | 2,792                               | 4,490        | 9,764                              | 13,044       |
| Loss on disposal and impairment of assets   | 6,747                               | 16,637       | 10,013                             | 22,040       |
| Total operating expenses  | 1,097,207                           | 1,027,256    | 3,155,547                          | 2,865,807    |
| Income from operations  | 30,867                              | 9,726        | 210,765                            | 4,017        |
| Interest and other income, net  | 1,275                               | 672          | 3,512                              | 3,584        |
| Income before income taxes  | 32,142                              | 10,398       | 214,277                            | 7,601        |
| Provision for income taxes  | (12,532)                            | (2,599)      | (81,817)                           | (638)        |
| Net income  | \$ 19,610                           | \$ 7,799     | \$ 132,460                         | \$ 6,963     |
| Earnings per share:   |                                     |              |                                    |              |
| Basic   | \$ 0.69                             | \$ 0.27      | \$ 4.63                            | \$ 0.24      |
| Diluted   | \$ 0.69                             | \$ 0.27      | \$ 4.62                            | \$ 0.23      |
| Weighted average common shares outstanding:   |                                     |              |                                    |              |
| Basic   | 28,415                              | 29,063       | 28,604                             | 29,387       |
| Diluted   | 28,439                              | 29,171       | 28,696                             | 29,792       |

Condensed Consolidated Statement of Comprehensive Income

(unaudited)

(in thousands)

|   | Three months<br>ended September<br>30, |          | Nine months ended<br>September 30, |          |
|---|--|----------|------------------------------------|----------|
|   | 2017                                   | 2016     | 2017                               | 2016     |
| Net income  | \$ 19,610                              | \$ 7,799 | \$ 132,460                         | \$ 6,963 |
| Other comprehensive income (loss), net of income taxes: |  |          |                                    |          |
| Foreign currency translation adjustments                | 1,778                                  | (203)    | 4,589                              | 961      |
| Unrealized gain (loss) on available-for-sale securities | 272                                    | (882)    | (99)                               | 3,051    |
| Tax benefit (expense)                                   | (104)                                  | 346      | 27                                 | (1,185)  |
| Other comprehensive income (loss), net of income taxes  | 1,946                                  | (739)    | 4,517                              | 2,827    |
| Comprehensive income                                    | \$ 21,556                              | \$ 7,060 | \$ 136,977                         | \$ 9,790 |

See accompanying notes to condensed consolidated financial statements.

Table of Contents

Chipotle Mexican Grill, Inc.

Condensed Consolidated Statement of Cash Flows

(unaudited)

(in thousands)



Edgar Filing: CHIPOTLE MEXICAN GRILL INC - Form 10-Q

|   | Nine months ended September 30,<br>2017 | 2016      |
|---|---|-----------|
| Operating activities  |   |           |
| Net income  | \$ 132,460                              | \$ 6,963  |
| Adjustments to reconcile net income to net cash provided by operating activities: |   |           |
| Depreciation and amortization   | 121,906                                 | 108,296   |
| Deferred income tax (benefit) provision   | (11,323)                                | 380       |
| Loss on disposal and impairment of assets   | 10,013                                  | 22,040    |
| Bad debt allowance  | 181                                     | 99        |
| Stock-based compensation expense  | 54,596                                  | 48,389    |
| Excess tax benefit on stock-based compensation                                    | -                                       | (1,888)   |
| Other   | (126)                                   | (224)     |
| Changes in operating assets and liabilities:                                      |   |           |
| Accounts receivable   | 16,477                                  | 16,084    |
| Inventory   | (7,023)                                 | (3,442)   |
| Prepaid expenses and other current assets   | (4,890)                                 | (5,362)   |
| Other assets  | (1,382)                                 | 1,509     |
| Accounts payable  | 14,771                                  | (11,938)  |
| Accrued liabilities   | 35,514                                  | 36,245    |
| Income tax payable/receivable   | (7,810)                                 | 36,026    |
| Deferred rent   | 22,410                                  | 27,319    |
| Other long-term liabilities   | 3,060                                   | 576       |
| Net cash provided by operating activities   | 378,834                                 | 281,072   |
| Investing activities  |   |           |
| Purchases of leasehold improvements, property and equipment                       | (165,506)                               | (192,252) |
| Purchases of investments  | (120,084)                               | -         |
| Maturities of investments   | 140,000                                 | 45,000    |
| Proceeds from sale of investments   | -                                       | 540,648   |
| Net cash provided by (used in) investing activities                               | (145,590)                               | 393,396   |
| Financing activities  |   |           |
| Acquisition of treasury stock   | (209,585)                               | (771,354) |
| Excess tax benefit on stock-based compensation                                    | -                                       | 1,888     |

|  |            |            |
|--|------------|------------|
| Stock plan transactions and other financing activities       | 10         | 23         |
| Net cash used in financing activities                        | (209,575)  | (769,443)  |
| Effect of exchange rate changes on cash and cash equivalents | 1,931      | 1,098      |
| Net change in cash and cash equivalents                      | 25,600     | (93,877)   |
| Cash and cash equivalents at beginning of period             | 87,880     | 248,005    |
| Cash and cash equivalents at end of period                   | \$ 113,480 | \$ 154,128 |

See accompanying notes to condensed consolidated financial statements.

Table of Contents

Chipotle Mexican Grill, Inc.

Notes to Condensed Consolidated Financial Statements

(unaudited)

(dollar and share amounts in thousands, unless otherwise specified)

1. Basis of Presentation

In this quarterly report on Form 10-Q, Chipotle Mexican Grill, Inc., a Delaware corporation, together with its subsidiaries, is collectively referred to as “Chipotle,” “we,” “us,” or “our.”

We develop and operate restaurants that serve a focused menu of burritos, tacos, burrito bowls, and salads, made using fresh, high-quality ingredients. As of September 30, 2017, we operated 2,330 Chipotle restaurants throughout the United States as well as 36 international Chipotle restaurants and 8 non-Chipotle restaurants. We managed our operations based on 11 regions during the third quarter of 2017 and have aggregated our operations to one reportable segment.

We have prepared the accompanying unaudited condensed consolidated financial statements in accordance with U.S. generally accepted accounting principles for interim financial statements and pursuant to the rules and regulations of the Securities and Exchange Commission. In the opinion of management, the accompanying unaudited condensed consolidated financial statements reflect all adjustments consisting of normal recurring adjustments necessary for a fair presentation of our financial position and results of operations. Interim results of operations are not necessarily indicative of the results that may be achieved for the full year. The financial statements and related notes do not include all information and footnotes required by U.S. generally accepted accounting principles for annual reports. This quarterly report should be read in conjunction with the consolidated financial statements included in our annual report on Form 10-K for the year ended December 31, 2016.

2. Recent Accounting Standards

Recently Issued Accounting Standards

In February 2016, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2016-02, “Leases (Topic 842).” The pronouncement requires lessees to recognize a liability for lease obligations, which represent the discounted obligation to make future minimum lease payments, and a corresponding right-of-use asset on the balance sheet. The guidance requires disclosure of key information about leasing arrangements which are intended to give financial statement users the ability to assess the amount, timing, and potential uncertainty of cash flows related to leases. We expect to adopt the requirements of the new lease standard effective January 1, 2019, using a modified retrospective adoption method. We are currently evaluating the provisions of the new lease standard, including optional practical expedients, and assessing our existing lease portfolio in order to determine the impact to our accounting systems, processes and internal control over financial reporting. The adoption of ASU 2016-02 will have a significant impact on our consolidated balance sheet because we will record material assets and obligations for current operating leases. We are still assessing the expected impact on our consolidated statements of income and cash flows.

In May 2014, the FASB issued ASU No. 2014-09, "Revenue from Contracts with Customers (Topic 606)," as amended by multiple standards updates. This guidance requires an entity to recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Additionally, this guidance will require us to enhance our disclosures, including disclosing performance obligations to customers arising from gift cards and certain promotional activity. The pronouncement is effective for reporting periods beginning after December 15, 2017. The adoption is not expected to have an impact on our consolidated financial position or results of operations.

We reviewed all other recently issued accounting pronouncements and concluded that they were either not applicable or not expected to have a significant impact on the consolidated financial statements.

#### Recently Adopted Accounting Standards

In March 2016, the FASB issued ASU 2016-09, "Compensation-Stock Compensation (Topic 718)." The pronouncement was issued to simplify several aspects of the accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities and classification on the condensed consolidated statement of cash flows.

We adopted ASU 2016-09 on January 1, 2017, prospectively (prior periods have not been restated). The primary impact of adoption was the recognition during the three months ended September 30, 2017, of a \$77 tax deficiency, which increases our provision for income taxes and for the nine months ended September 30, 2017, an excess tax benefit of \$587, which reduces our provision for income taxes and the classification of these excess tax benefits in operating activities in the condensed consolidated statement of cash flows instead of financing activities.

Table of Contents

The presentation requirements for cash flows related to employee taxes paid for withheld shares had no impact to any of the periods presented in the condensed consolidated statement of cash flows, since such cash flows have historically been presented in financing activities. We also elected to continue estimating forfeitures when determining the amount of stock-based compensation costs to be recognized in each period. No other provisions of ASU 2016-09 had a material impact on our financial statements or disclosures.

### 3. Fair Value of Financial Instruments

The carrying value of our cash and cash equivalents, accounts receivable and accounts payable approximate fair value because of their short-term nature. Investments are carried at fair value and are classified as available-for-sale. Investments consist of U.S. treasury notes with maturities up to approximately one year. Fair value of investments is measured using Level 1 inputs (quoted prices for identical assets in active markets).

The following is a summary of available-for-sale securities:

|                           | September<br>30,<br>2017 | December<br>31,<br>2016 |
|---------------------------|--------------------------|-------------------------|
| Amortized cost            | \$ 435,193               | \$ 455,109              |
| Unrealized gains (losses) | (316)                    | (218)                   |
| Fair market value         | \$ 434,877               | \$ 454,891              |

The following is a summary of unrealized gains (losses) on available-for-sale securities recorded in other comprehensive income (loss) in the condensed consolidated statement of comprehensive income:

|  | Three months<br>ended<br>September 30,<br>2017 |          | Nine months<br>ended<br>September 30,<br>2016 |          |
|--|--|----------|---|----------|
| Unrealized gains (losses) on available-for-sale securities             | \$ 272   | \$ (882) | \$ (99)                                       | \$ 3,051 |
| Unrealized gains (losses) on available-for-sale securities, net of tax | \$ 168   | \$ (536) | \$ (72)                                       | \$ 1,866 |

Realized gains and losses on available-for-sale securities are recorded in interest and other income, net on the condensed consolidated statement of income. We had no realized gains or losses for the three and nine months ended September 30, 2017, and we had \$0 and \$547 of realized gains on available-for-sale securities for the three and nine months ended September 30, 2016.

We also maintain a rabbi trust to fund obligations under a deferred compensation plan. Amounts in the rabbi trust are invested in mutual funds, which are designated as trading securities and carried at fair value, and are included in other assets in the condensed consolidated balance sheet. Fair value of mutual funds is measured using Level 1 inputs. The fair value of the investments in the rabbi trust was \$19,157 and \$17,843 as of September 30, 2017, and December 31,

2016, respectively. We record trading gains and losses in general and administrative expenses in the condensed consolidated statement of income, along with the offsetting amount related to the increase or decrease in deferred compensation to reflect our exposure to liabilities for payment under the deferred plan.

The following table sets forth unrealized gains (losses) on trading securities held in the rabbi trust:

|   | Three months<br>ended<br>September 30, |        | Nine months<br>ended<br>September 30, |        |
|---|--|--------|---------------------------------------|--------|
|   | 2017                                   | 2016   | 2017                                  | 2016   |
| Unrealized gains (losses) on trading securities held in rabbi trust | \$ 335                                 | \$ 391 | \$ 1,157                              | \$ 677 |

#### 4. Impairment of Long-Lived Assets

During the three and nine months ended September 30, 2017, we recognized non-cash impairment charges of \$2,427 and \$4,441 (\$1,475 and \$2,699 net of tax, respectively), representing substantially all of the value of the long-lived assets of a small number of underperforming Chipotle restaurants, in loss on disposal and impairment of assets on the condensed consolidated statement of income (\$0.05 and \$0.09 per basic and diluted earnings per share). The fair value of the impaired restaurants was determined using Level 3 inputs (unobservable inputs) based on a discounted cash flow method.

Table of Contents

5. Shareholders' Equity

Through September 30, 2017, we had announced authorizations by our Board of Directors of repurchases of shares of common stock, which in the aggregate authorized expenditures of up to \$2.3 billion. On October 24, 2017, we announced that our Board of Directors authorized the expenditure of an additional \$100,000 to repurchase shares of common stock. Under the remaining repurchase authorizations, shares may be purchased from time to time in open market transactions, subject to market conditions.

During the nine months ended September 30, 2017, we repurchased 545 shares of common stock under authorized programs, for a total cost of \$207,159. The cumulative shares repurchased under authorized programs as of September 30, 2017, were 7,408 for a total cost of \$2,204,968. As of September 30, 2017, \$95,425 was available to repurchase shares under the announced repurchase authorizations. Shares repurchased are being held in treasury stock until such time as they are reissued or retired at the discretion of the Board of Directors.

6. Stock-based Compensation

During the nine months ended September 30, 2017, we granted stock only stock appreciation rights ("SOSARs") on 304 shares of our common stock to eligible employees. The weighted average grant date fair value of the SOSARs was \$105.97 per share with a weighted average exercise price of \$426.70 per share based on the closing price of common stock on the date of grant. The SOSARs vest in two equal installments on the second and third anniversary of the grant date. During the nine months ended September 30, 2017, 32 SOSARs were exercised and 124 SOSARs were forfeited.

During the nine months ended September 30, 2017, we granted restricted stock units ("RSUs") on 89 shares of our common stock to eligible employees. The weighted average grant date fair value of the RSUs was \$427.30 per share. The RSUs generally vest in two equal installments on the second and third anniversary of the grant date.

During the first quarter of 2017, we awarded 36 performance shares ("PSUs") that are subject to service, market and performance vesting conditions. Two-thirds of the PSUs had a grant date fair value of \$485.53 per share and vest based on the price of our common stock reaching certain targets for a consecutive number of days during the three-year period starting on the grant date and the quantity of shares that will vest range from 0% to 350% of the targeted number of shares. The remaining one-third of PSUs had a grant date fair value of \$427.61 and vest based on reaching certain comparable restaurant sales increases during the three-year period starting on January 1, 2017, and the quantity of shares that will vest range from 0% to 300% of the targeted number of shares. If the defined minimum targets are not met, then no shares will vest.

During the nine months ended September 30, 2017, 20 stock awards that were subject to service and performance or market conditions were forfeited.

The following table sets forth total stock based compensation expense:

|  | Three months ended<br>September 30, |           | Nine months ended<br>September 30, |           |
|--|-------------------------------------|-----------|------------------------------------|-----------|
|  | 2017                                | 2016      | 2017                               | 2016      |
| Stock based compensation expense   | \$ 18,069                           | \$ 18,636 | \$ 55,545                          | \$ 49,357 |
| Stock based compensation expense, net of tax   | \$ 10,983                           | \$ 10,971 | \$ 33,760                          | \$ 29,056 |
| Stock based compensation expense recognized as capitalized development                               | \$ 319                              | \$ 285    | \$ 949                             | \$ 968    |
| Excess tax benefit (deficiency) on stock based compensation recognized in provision for income taxes | \$ (77)                             | \$ -      | \$ 587                             | \$ -      |

## 7. Earnings Per Share

Basic earnings per share is calculated by dividing income available to common shareholders by the weighted-average number of shares of common stock outstanding during each period. Diluted earnings per share (“diluted EPS”) is calculated using income available to common shareholders divided by diluted weighted-average shares of common stock outstanding during each period. Potentially dilutive securities include common shares related to SOSARs and non-vested stock awards (collectively “stock awards”). Diluted EPS considers the impact of potentially dilutive securities except in periods in which there is a loss because the inclusion of the potential common shares would have an antidilutive effect. Stock awards are excluded from the calculation of diluted EPS in the event they are subject to performance conditions or are antidilutive.



Table of Contents

The following stock awards were excluded from the calculation of diluted earnings per share:

|   | Three months<br>ended September<br>30, |       | Nine months<br>ended September<br>30, |       |
|---|--|-------|---------------------------------------|-------|
|   | 2017                                   | 2016  | 2017                                  | 2016  |
| Stock awards subject to performance conditions              | 245                                    | 226   | 244                                   | 276   |
| Stock awards that were antidilutive                         | 1,738                                  | 1,356 | 1,567                                 | 1,312 |
| Total stock awards excluded from diluted earnings per share | 1,983                                  | 1,582 | 1,811                                 | 1,588 |

The following table sets forth the computations of basic and diluted earnings per share:

|  | Three months ended<br>September 30, |          | Nine months ended<br>September 30, |          |
|--|-------------------------------------|----------|------------------------------------|----------|
|  | 2017                                | 2016     | 2017                               | 2016     |
| Net income   | \$ 19,610                           | \$ 7,799 | \$ 132,460                         | \$ 6,963 |
| Shares:  |                                     |          |                                    |          |
| Weighted average number of common shares outstanding         | 28,415                              | 29,063   | 28,604                             | 29,387   |
| Dilutive stock awards  | 24                                  | 108      | 92                                 | 405      |
| Diluted weighted average number of common shares outstanding | 28,439                              | 29,171   | 28,696                             | 29,792   |
| Basic earnings per share                                     | \$ 0.69                             | \$ 0.27  | \$ 4.63                            | \$ 0.24  |
| Diluted earnings per share                                   | \$ 0.69                             | \$ 0.27  | \$ 4.62                            | \$ 0.23  |

## 8. Commitments and Contingencies

### Data Security Incident

In April 2017, our information security team detected unauthorized activity on the network that supports payment processing for our restaurants, and immediately began an investigation with the help of leading computer security firms. We also self-reported the issue to payment card processors and law enforcement. Our investigation detected malware designed to access payment card data from cards used at point-of-sale devices at most Chipotle restaurants,

primarily in the period from March 24, 2017 through April 18, 2017. The malware searched for track data, which may include cardholder name, card number, expiration date, and internal verification codes; however, no other customer information was affected. We have removed the malware from our systems and continue to evaluate ways to enhance our security measures. We expect that substantially all of our investigation costs will be covered by insurance; however, we may incur legal expenses in excess of our insurance coverage limits associated with the data security incident in future periods. We will recognize these expenses as services are received.

During the three months ended September 30, 2017, we recorded an expense of \$30,000 (\$18,234 after tax), or \$0.64 per basic and diluted earnings per share, as an estimate of potential liabilities associated with anticipated claims and assessments by payment card networks in connection with the data security incident. We may ultimately be subject to liabilities greater than or less than the amount accrued. The expense is recorded in general and administrative expenses in our condensed consolidated statement of income and a corresponding liability in accrued liabilities on our condensed consolidated balance sheet.

#### Litigation Arising from Security Incident

On May 4, 2017, Bellwether Community Credit Union filed a purported class action complaint in the United States District Court for the District of Colorado alleging that we negligently failed to provide adequate security to protect the payment card information of customers of the plaintiffs and those of other similarly situated credit unions, banks and other financial institutions alleged to be part of the putative class, causing those institutions to suffer financial losses. The complaint also claims we were negligent per se based on alleged violations of Section 5 of the Federal Trade Commission Act and similar state laws. The plaintiff seeks monetary damages, injunctive relief and attorneys' fees. On May 26, 2017, Alcoa Community Credit Union filed a purported class action complaint in the U. S. District Court for the District of Colorado making substantially the same allegations as the Bellwether complaint and seeking substantially the same relief. The Bellwether and Alcoa cases have been consolidated and will proceed as a single action.

On June 9, 2017, Todd Gordon filed a purported class action complaint in the U. S. District Court for the District of Colorado alleging that we negligently failed to provide adequate security to protect the payment card information of the plaintiff and other similarly situated customers alleged to be part of the putative class, causing such customers to suffer financial losses. The complaint also claims we were negligent per se

## Table of Contents

based on alleged violations of Section 5 of the Federal Trade Commission Act and similar state laws, and also alleges breach of contract, unjust enrichment, and violations of the Arizona Consumer Fraud Act. Additionally, on August 21, 2017, Greg Lawson and Judy Conard filed a purported class action complaint in the U. S. District Court for the District of Colorado making allegations substantially similar to those in the Gordon complaint, and stating substantially similar claims as well as claims under the Colorado Consumer Protection Act. The plaintiffs in the Gordon case and the Lawson and Conard case have notified the court of their agreement to consolidate their cases and file an amended consolidated complaint for the consolidated matter.

We intend to vigorously defend each of the aforementioned cases, but it is not possible at this time to reasonably estimate the outcome of or any potential liability from these cases. Although certain fees and costs associated with the data security incident and the aforementioned litigation to date have been paid or reimbursed by our cyber liability insurer, the ultimate amount of liabilities arising from the litigation may be in excess of the limits of our applicable insurance coverage.

### Receipt of Grand Jury Subpoenas

On January 28, 2016, we were served with a Federal Grand Jury Subpoena from the U.S. District Court for the Central District of California in connection with an official criminal investigation being conducted by the U.S. Attorney's Office for the Central District of California, in conjunction with the U.S. Food and Drug Administration's Office of Criminal Investigations. The subpoena requires the production of documents and information related to company-wide food safety matters dating back to January 1, 2013. We received a follow-up subpoena on July 19, 2017 requesting information related to illness incidents associated with a single Chipotle restaurant in Sterling, Virginia. We intend to continue to fully cooperate in the investigation. It is not possible at this time to determine whether we will incur, or to reasonably estimate the amount of, any fines or penalties in connection with the investigation pursuant to which the subpoena was issued.

### Shareholder Derivative Actions

On April 6, 2016, Uri Skorski filed a shareholder derivative action in Colorado state court in Denver, Colorado, alleging that our Board of Directors and officers breached their fiduciary duties in connection with our alleged failure to disclose material information about our food safety policies and procedures, and also alleging that our Board of Directors and officers breached their fiduciary duties in connection with allegedly excessive compensation awarded from 2011 to 2015 under our stock incentive plan. On April 14, 2016, Mark Arnold and Zachary Arata filed a shareholder derivative action in Colorado state court in Denver, Colorado, making largely the same allegations as the Skorski complaint. On May 26, 2016, the court issued an order consolidating the Skorski and Arnold/Arata actions into a single case. On August 8, 2016, Sean Gubricky filed a shareholder derivative action in the U.S. District Court for the District of Colorado, alleging that our Board of Directors and certain officers failed to institute proper food safety controls and policies, issued materially false and misleading statements in violation of federal securities laws, and otherwise breached their fiduciary duties to us. On September 1, 2016, Ross Weintraub filed a shareholder derivative action in Colorado state court in Denver, Colorado, making largely the same allegations as the Gubricky complaint. On March 27, 2017, the Weintraub case was consolidated with the Skorski and Arnold/Arata action into a single case. On December 27, 2016, Cyrus Lashkari filed a shareholder derivative action in the U.S. District Court for the District of Colorado, making largely the same allegations as the foregoing shareholder derivative complaints. Each of these actions purports to state a claim for damages on our behalf, and is based on statements in our SEC filings and related public disclosures, as well as media reports and company records. We have reached an agreement to settle the foregoing actions, and the proposed settlement has been preliminarily approved by the U.S. District Court for the District of Colorado.

On July 28, 2017, Mark Blau filed a shareholder derivative action in the U.S. District Court for the District of Colorado, making allegations similar to those of the several shareholder derivative actions described above, and adding further allegations related to the Board's investigation of the foregoing matters, as well as customer illnesses and operational issues associated with two Chipotle restaurants in July 2017. The action purports to state claims for damages on our behalf, and is based on statements in our SEC filings and related public disclosures, as well as media reports and company records. We intend to defend this case vigorously, but it is not possible at this time to reasonably estimate the outcome of or any potential liability from the case.

#### Shareholder Class Actions

On January 8, 2016, Susie Ong filed a complaint in the U.S. District Court for the Southern District of New York on behalf of a purported class of purchasers of shares of our common stock between February 4, 2015 and January 5, 2016. The complaint purports to state claims against us, each of the co-Chief Executive Officers serving during the claimed class period and the Chief Financial Officer under Sections 10(b) and 20(a) of the Exchange Act and related rules, based on our alleged failure during the claimed class period to disclose material information about our quality controls and safeguards in relation to consumer and employee health. The complaint asserts that those failures and related public statements were false and misleading and that, as a result, the market price of our stock was artificially inflated during the claimed class period. The complaint seeks damages on behalf of the purported class in an unspecified amount, interest, and an award of reasonable attorneys' fees, expert fees and other costs. On March 8, 2017, the court granted our motion to dismiss the complaint, with leave to amend. The plaintiff filed an amended complaint on April 7, 2017. Additionally, on July 20, 2017, Elizabeth Kelly filed a complaint in the U.S. District Court for the District of Colorado on behalf of a purported class of purchasers of shares of our common stock between February 5, 2016 and July 19, 2017,

Table of Contents

with claims and factual allegations similar to the Ong complaint, based primarily on media reports regarding illnesses associated with a Chipotle restaurant in Sterling, Virginia. We intend to defend these cases vigorously, but it is not possible at this time to reasonably estimate the outcome of or any potential liability from the cases.

Miscellaneous

We are involved in various other claims and legal actions that arise in the ordinary course of business. We do not believe that the ultimate resolution of these actions will have a material adverse effect on our financial position, results of operations, liquidity or capital resources. However, a significant increase in the number of these claims, or one or more successful claims under which we incur greater liabilities than we currently anticipate, could materially and adversely affect our business, financial condition, results of operations and cash flows.

## Table of Contents

### ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

#### Cautionary Note Regarding Forward-Looking Statements

Certain statements in this report, including projections of our expected comparable restaurant sales increases for 2017, projected new restaurant openings for 2017 and 2018, discussion of the potential impacts of our roll-out of queso and of menu price increases, projections of expected changes in food, beverage and packaging costs and marketing and promotional spend, estimates of our effective tax rates, and discussion of liabilities associated with the recent data security incident, are forward-looking statements as defined in the Private Securities Litigation Reform Act of 1995. We use words such as “anticipate”, “believe”, “could”, “should”, “estimate”, “expect”, “intend”, “may”, “predict”, “project”, “similar terms and phrases, including references to assumptions, to identify forward-looking statements. These forward-looking statements are based on information available to us as of the date any such statements are made, and we assume no obligation to update these forward-looking statements. These statements are subject to risks and uncertainties that could cause actual results to differ materially from those described in the statements. These risks and uncertainties include, but are not limited to, the risk factors described in our annual report on Form 10-K for the year ended December 31, 2016, as updated in Part II, Item 1A. of this report.

#### Overview

Steve Ells, our founder, Chairman and CEO, started Chipotle with the idea that food served fast did not have to be a typical fast food experience. Today, Chipotle continues to offer a focused menu of burritos, tacos, burrito bowls, and salads made from fresh, high-quality raw ingredients, prepared using classic cooking methods and served in an interactive style allowing our customers to get what they want. Chipotle seeks out extraordinary ingredients that are not only fresh, but that are raised responsibly, with respect for the animals, land, and people who produce them. Chipotle prepares its food using real, whole ingredients and without the use of added colors, flavors or other additives typically found in fast food.

Throughout our history as a public company, we have pursued a mission to change the way people think about and eat fast food. We have expanded our mission to: Ensure that better food, prepared from whole, unprocessed ingredients is accessible to everyone. Additionally, our focus during 2017 is to return to sales and profitability growth and restore our restaurant economic model. To do so, we have a renewed focus on ensuring that every guest in every one of our restaurants is provided with an excellent customer experience.

#### 2017 Highlights

**Sales Trends.** Comparable restaurant sales increases were 1.0% and 8.3% for the three and nine months ended September 30, 2017, respectively. Our sales comparisons for the first nine months of 2017 were lapping an easier comparison due to lower sales levels in the first six months of 2016. Additionally, sales comparisons for the three and nine months ended September 30, 2017, benefitted from lower revenue in the comparable periods of 2016 due to revenue deferrals for outstanding rewards under our limited-time Chiptopia Summer Rewards program (though the first quarter 2017 also benefitted from the recognition of a portion of the deferred revenue). During the third quarter of 2017, increases in comparable restaurant sales were offset by adverse company-wide sales impacts resulting from news regarding a norovirus incident in Sterling, Virginia, and to a lesser extent due to restaurant closures and lower customer traffic resulting from Hurricanes Harvey and Irma. We expect full year 2017 comparable restaurant sales increases to be around 6.5% including impacts from a menu price increase planned for the fourth quarter of 2017 and the roll-out of queso. Comparable restaurant sales represent the change in period-over-period sales for restaurants

beginning in their 13th full calendar month of operation. Average restaurant sales were \$1.948 million as of September 30, 2017, increasing from \$1.914 million as of September 30, 2016, but a decrease from \$1.957 million as of June 30, 2017. We define average restaurant sales as the average trailing 12-month sales for restaurants in operation for at least 12 full calendar months.

**Restaurant Operating Costs.** Our restaurant operating costs (food, beverage and packaging; labor; occupancy; and other operating costs) as a percentage of revenue decreased to 82.4% in the first nine months of 2017, as compared to 87.5% in the first nine months of 2016. The decrease was primarily due to lower marketing and promotional spend, sales leverage, labor efficiencies, and lower food costs. Food costs were lower in the first nine months of 2017 despite significantly higher pricing of avocados during the third quarter of 2017.

**Restaurant Development.** As of September 30, 2017, we had 2,374 restaurants in operation, including 2,330 Chipotle restaurants throughout the United States, 36 international Chipotle restaurants and 8 non-Chipotle restaurants. We opened 145 restaurants and we closed or relocated 21 restaurants during the nine months ended September 30, 2017, including the closure of all 15 ShopHouse Southeast Asian Kitchen restaurants. We expect new restaurant openings for the full year 2017 to be slightly below the low end of our previously-disclosed range of 195 to 210. For 2018, we expect new restaurant openings in a range of approximately 130 to 150, as we focus our resources for the next 12 to 18 months on improving our operations and delivering an outstanding experience to every one of our guests.

**Data Security Incident.** As previously reported, in April 2017, our information security team detected unauthorized activity on the network that supports payment processing for our restaurants, and immediately began an investigation with the help of leading computer security firms. The investigation detected malware designed to access payment card data from cards used at point-of-sale devices at most Chipotle restaurants.

Table of Contents

The malware searched for track data, which may include cardholder name, card number, expiration date, and internal verification codes; however, no other customer information was affected. We have removed the malware from our systems and continue to evaluate ways to enhance our security measures.

During the three months ended September 30, 2017, we recorded a liability of \$30.0 million (\$18.2 million after tax) or \$0.64 per basic and diluted earnings per share, as an estimate of potential losses associated with anticipated claims and assessments by payment card networks. We may ultimately be subject to liabilities greater or less than the amount accrued. In addition, legal claims have been made against us related to this matter, and are further discussed in Note 8. "Commitments and Contingencies" within Item 1. "Financial Statements."

## Restaurant Activity

The following table details restaurant unit data for the periods indicated:

|                                    | Three months ended<br>September<br>30, |       | Nine months ended<br>September<br>30, |       |
|------------------------------------|--|-------|---------------------------------------|-------|
|                                    | 2017                                   | 2016  | 2017                                  | 2016  |
| Beginning of period                | 2,339                                  | 2,124 | 2,250                                 | 2,010 |
| Openings                           | 38                                     | 55    | 145                                   | 171   |
| Relocations/closures               | (3)                                    | (1)   | (6)                                   | (3)   |
| ShopHouse closures                 | -                                      | -     | (15)                                  | -     |
| Total restaurants at end of period | 2,374                                  | 2,178 | 2,374                                 | 2,178 |

## Results of Operations

Our results of operations as a percentage of revenue and period-over-period changes are discussed in the following section. As our business grows and we open more restaurants and hire more employees, our aggregate restaurant operating costs and depreciation and amortization generally increase.

## Revenue

|   | Three months ended<br>September 30, |            |               | Nine months ended<br>September 30, |            |               |
|---|-------------------------------------|------------|---------------|------------------------------------|------------|---------------|
|   | 2017                                | 2016       | %<br>increase | 2017                               | 2016       | %<br>increase |
|   | (dollars in millions)               |            |               | (dollars in millions)              |            |               |
| Revenue   | \$ 1,128.1                          | \$ 1,037.0 | 8.8%          | \$ 3,366.3                         | \$ 2,869.8 | 17.3%         |
| Average restaurant sales                          | \$ 1,948                            | \$ 1,914   | 1.8%          | \$ 1,948                           | \$ 1,914   | 1.8%          |
| Comparable restaurant sales increases (decreases) | 1.0%                                | (21.9%)    |               | 8.3%                               | (24.9%)    |               |
| Number of restaurants as of the end of the period | 2,374                               | 2,178      | 9.0%          | 2,374                              | 2,178      | 9.0%          |
| Number of restaurants opened in the period        | 38                                  | 55         |               | 145                                | 171        |               |



The most significant factor contributing to the increase in revenue for the three months ended September 30, 2017, was \$84.9 million in revenue from restaurants not yet in the comparable base, of which \$46.1 million was attributable to restaurants opened in 2017. Comparable restaurant sales increased \$6.2 million. For the nine months ended September 30, 2017, revenue from restaurants not yet in the comparable restaurant base contributed \$268.0 million to the revenue increase, of which \$91.3 million was attributable to restaurants opened in 2017, and comparable restaurant sales increased \$228.4 million. For the nine months ended September 30, 2017, the increase in comparable restaurant sales was attributable to an increase in the number of paid transactions and an increase in paid average check due to fewer promotions during the first nine months of 2017.

#### Food, Beverage and Packaging Costs

|                              | Three months ended    |                       |               | Nine months ended     |                       |               |
|------------------------------|-----------------------|-----------------------|---------------|-----------------------|-----------------------|---------------|
|                              | September 30,<br>2017 | September 30,<br>2016 | %<br>increase | September 30,<br>2017 | September 30,<br>2016 | %<br>increase |
|                              | (dollars in millions) |                       |               | (dollars in millions) |                       |               |
| Food, beverage and packaging | \$ 394.6              | \$ 363.9              | 8.4%          | \$ 1,155.5            | \$ 1,000.0            | 15.6%         |
| As a percentage of revenue   | 35.0%                 | 35.1%                 |               | 34.3%                 | 34.8%                 |               |

Table of Contents

Food, beverage and packaging costs remained consistent as a percentage of revenue for the three months ended September 30, 2017. The benefit of the menu price increases taken in select restaurants during the second quarter of 2017 and decreased paper cost and usage were offset by higher avocado and beef prices, as well as steak making up a higher portion of our product mix compared to the third quarter of 2016. The decrease in food, beverage and packing costs as a percentage of revenue for the nine months ended September 30, 2017, was due primarily bringing the preparation of lettuce and bell peppers back into our restaurants after using pre-cut produce during portions of 2016, reduced testing and waste costs, and the benefit of the menu price increase that went into effect during the second quarter of 2017. The decrease was partially offset by higher avocado prices. Lower projected avocado prices are expected to drive decreased food costs as a percentage of revenue during the fourth quarter of 2017, and we expect food costs for the full year to be consistent with the first nine months of 2017.

## Labor Costs

|                            | Three months ended    |          |               | Nine months ended     |          |            |
|----------------------------|-----------------------|----------|---------------|-----------------------|----------|------------|
|                            | September 30,<br>2017 | 2016     | %<br>increase | September 30,<br>2017 | 2016     | % increase |
|                            | (dollars in millions) |          |               | (dollars in millions) |          |            |
| Labor costs                | \$ 306.9              | \$ 286.1 | 7.2%          | \$ 900.6              | \$ 820.8 | 9.7%       |
| As a percentage of revenue | 27.2%                 | 27.6%    |               | 26.8%                 | 28.6%    |            |

Labor costs as a percentage of revenue decreased for the three months ended September 30, 2017, primarily due to labor efficiencies resulting from more efficient crew deployment and fewer managers in each of our restaurants, partially offset by wage inflation. Labor costs as a percentage of revenue decreased for the nine months ended September 30, 2017 due to labor efficiencies from more efficient crew deployment and fewer managers in each of our restaurants, as well as sales leverage, partially offset by wage inflation. Labor efficiencies in the three and nine months ended September 30, 2017 benefitted from abnormally high labor expenses in the comparable 2016 periods as a result of being fully staffed during the heavy sales promotional activity we were conducting during those periods.

## Occupancy Costs

|                            | Three months                   |         |               | Nine months                    |          |            |
|----------------------------|--------------------------------|---------|---------------|--------------------------------|----------|------------|
|                            | ended September<br>30,<br>2017 | 2016    | %<br>increase | ended September<br>30,<br>2017 | 2016     | % increase |
|                            | (dollars in<br>millions)       |         |               | (dollars in<br>millions)       |          |            |
| Occupancy costs            | \$ 83.2                        | \$ 74.2 | 12.1%         | \$ 242.5                       | \$ 217.1 | 11.7%      |
| As a percentage of revenue | 7.4%                           | 7.2%    |               | 7.2%                           | 7.6%     |            |

Occupancy costs as a percentage of revenue increased for the three months ended September 30, 2017, primarily due to lower average daily restaurant sales due to new restaurants opening at lower sales volumes than restaurants in the comparable base, and those sales volumes being applied across a partially fixed-cost base. Occupancy costs as a percentage of revenue decreased for the nine months ended September 30, 2017, primarily due to sales leverage on a partially fixed-cost base.

#### Other Operating Costs

|                            | Three months ended    |          |               | Nine months ended     |          |            |
|----------------------------|-----------------------|----------|---------------|-----------------------|----------|------------|
|                            | September 30,<br>2017 | 2016     | %<br>decrease | September 30,<br>2017 | 2016     | % increase |
|                            | (dollars in millions) |          |               | (dollars in millions) |          |            |
| Other operating costs      | \$ 162.3              | \$ 166.0 | (2.2%)        | \$ 476.6              | \$ 473.4 | 0.7%       |
| As a percentage of revenue | 14.4%                 | 16.0%    |               | 14.2%                 | 16.5%    |            |

Other operating costs include, among other items, marketing and promotional costs, bank and credit card fees, and restaurant utilities and maintenance costs. Other operating costs as a percentage of revenue decreased for the three and nine months ended September 30, 2017 due primarily to decreased marketing and promotional spend, and decreased kitchen supplies expense. While marketing and promotional spend decreased to 3.4% of revenue for the first nine months of 2017, as compared to 5.2% for the first nine months of 2016, it remains above historical levels as we continue our efforts to drive customer traffic. We expect to increase marketing and advertising expenses in the fourth quarter of 2017 as we continue national television advertising, and as a result, we expect full year 2017 other operating costs as a percentage of revenue to be higher in the fourth quarter and the full year 2017 than they were in the first nine months of 2017, but lower than the full year 2016.

Table of Contents

## General and Administrative Expenses

|                                    | Three months<br>ended September<br>30,<br>2017 |         |          | % | Nine months<br>ended September<br>30,<br>2017 |          |            |
|------------------------------------|--|---------|----------|---|---|----------|------------|
|                                    | 2016   |         | increase |   | 2016  |          | % increase |
|                                    | (dollars in<br>millions)                       |         |          |   | (dollars in<br>millions)                      |          |            |
| General and administrative expense | \$ 99.2  | \$ 78.4 | 26.5%    |   | \$ 238.7                                      | \$ 211.2 | 13.0%      |
| As a percentage of revenue         | 8.8%   | 7.6%    |          |   | 7.1%  | 7.4%     |            |

General and administrative expense increased during the three and nine months ended September 30, 2017, due to recording a liability of \$30.0 million, as an estimate of potential losses associated with anticipated claims and assessments by payment card networks, for the data security incident that occurred in the first six months of 2017. For the three months ended September 30, 2017, the increase was partially offset by a decrease in meeting costs because of the bi-annual All Managers Conference held in September 2016. Additionally, for the nine months ended September 30, 2017, higher non-cash stock-based compensation expense and increased bonus costs were more than offset by lower meeting and legal costs. The increase in stock-based compensation expense during 2017 was primarily a result of a cumulative reduction of expense in the first quarter of 2016 for performance share awards that were no longer expected to vest.

## Depreciation and Amortization

|                               | Three months<br>ended September<br>30,<br>2017 |         |          | % | Nine months<br>ended September<br>30,<br>2017 |          |            |
|-------------------------------|--|---------|----------|---|---|----------|------------|
|                               | 2016   |         | increase |   | 2016  |          | % increase |
|                               | (dollars in<br>millions)                       |         |          |   | (dollars in<br>millions)                      |          |            |
| Depreciation and amortization | \$ 41.5  | \$ 37.4 | 11.0%    |   | \$ 121.9                                      | \$ 108.3 | 12.6%      |
| As a percentage of revenue    | 3.7%   | 3.6%    |          |   | 3.6%  | 3.8%     |            |

For the three months ended September 30, 2017, depreciation and amortization remained relatively consistent as a percent of revenue. For the nine months ended September 30, 2017, depreciation and amortization decreased as a percentage of revenue due to sales leverage on a partially fixed-cost base.

## Loss on Disposal and Impairment of Assets

|   | Three months<br>ended September<br>30, |         |               | Nine months<br>ended September<br>30, |         |            |
|---|--|---------|---------------|---------------------------------------|---------|------------|
|   | 2017                                   | 2016    | %<br>decrease | 2017                                  | 2016    | % decrease |
|   | (dollars in<br>millions)               |         |               | (dollars in<br>millions)              |         |            |
| Loss on disposal and impairment of assets | \$ 6.7                                 | \$ 16.6 | (59.4%)       | \$ 10.0                               | \$ 22.0 | (54.6%)    |
| As a percentage of revenue                | 0.6%                                   | 1.6%    |               | 0.3%                                  | 0.8%    |            |

Loss on disposal and impairment of assets decreased in dollar terms for the three and nine months ended September 30, 2017 primarily due to a non-cash impairment charge in the third quarter of 2016 to write-down substantially all of the value of the long-lived assets of our ShopHouse restaurants that occurred during the third quarter of 2016. In 2017, we recorded losses related to the closure of a small number of underperforming Chipotle restaurants, the replacement of certain kitchen equipment, and assets that were damaged by natural disasters occurring during the quarter.

#### Provision for Income Taxes

|                            | Three months ended<br>September 30, |        |               | Nine months ended<br>September 30, |        |            |
|----------------------------|-------------------------------------|--------|---------------|------------------------------------|--------|------------|
|                            | 2017                                | 2016   | %<br>increase | 2017                               | 2016   | % increase |
|                            | (dollars in millions)               |        |               | (dollars in<br>millions)           |        |            |
| Provision for income taxes | \$ 12.5                             | \$ 2.6 | 382.2%        | \$ 81.8                            | \$ 0.6 | n/m*       |
| Effective tax rate         | 39.0%                               | 25.0%  |               | 38.2%                              | 8.4%   |            |

\*Not meaningful

For the full year 2017, we estimate our effective tax rate will be approximately 39.1% compared to 40.8% for the full year 2016. The lower 2017 estimated annual effective tax rate is due to a decrease in the state tax rate. The effective tax rate for the nine months ended September 30, 2017, is lower than the estimated annual rate due to non-recurring adjustments related to state income taxes and excess tax

## Table of Contents

deductions for stock compensation. The adoption on January 1, 2017, of ASU 2016-09 will subject our tax rate to quarterly volatility from the effect of stock award exercises and vesting activities.

### Seasonality

Seasonal factors cause our profitability to fluctuate from quarter to quarter. Historically, our average daily restaurant sales are lower and net income has generally been lower in the first and fourth quarters due, in part, to the holiday season and because fewer people eat out during periods of inclement weather (the winter months) than during periods of mild or warm weather (the spring, summer and fall months). Other factors also have a seasonal effect on our results. For example, restaurants located near colleges and universities generally do more business during the academic year. Seasonal factors, however, might be moderated or outweighed by other factors that may influence our quarterly results, such as unexpected publicity impacting our business in a positive or negative way, as well as fluctuations in food or packaging costs or the timing of menu price increases. The number of trading days in a quarter can also affect our results, although, on an overall annual basis, changes in trading days do not have a significant impact.

Our quarterly results are also affected by other factors such as the amount and timing of non-cash stock-based compensation expense, the number of new restaurants opened in a quarter, and anticipated and unanticipated events. New restaurants typically have lower margins following opening as a result of the expenses associated with opening new restaurants and their operating inefficiencies in the months immediately following opening. Accordingly, results for a particular quarter are not necessarily indicative of results to be expected for any other quarter or for any year.

### Liquidity and Capital Resources

Our primary liquidity and capital requirements are for new restaurant construction, working capital and general corporate needs. As of September 30, 2017, we had a cash and short-term investment balance of \$548.4 million that we expect to utilize, along with cash flow from operations, to provide capital to support the growth of our business (primarily through opening restaurants), to repurchase additional shares of our common stock subject to market conditions, to maintain our existing restaurants and for general corporate purposes. As of September 30, 2017, \$95.4 million remained available under previously-announced repurchase authorizations. On October 24, 2017, we announced that our Board of Directors authorized the expenditure of an additional \$100 million to repurchase shares of common stock. Under the remaining repurchase authorizations, shares may be purchased from time to time in open market transactions, subject to market conditions. We believe that cash from operations, together with our cash and investment balances, will be enough to meet ongoing capital expenditures, working capital requirements and other cash needs for the foreseeable future.

We haven't required significant working capital because customers generally pay using cash or credit and debit cards and because our operations do not require significant receivables, nor do they require significant inventories due, in part, to our use of various fresh ingredients. In addition, we generally have the right to pay for the purchase of food, beverage and supplies some time after the receipt of those items, generally within ten days, thereby reducing the need for incremental working capital to support our growth.

### Off-Balance Sheet Arrangements

As of September 30, 2017, we had no off-balance sheet arrangements or obligations.

### Critical Accounting Estimates

Critical accounting estimates are those that we believe are both significant and that require us to make difficult, subjective or complex judgments, often because we need to estimate the effect of inherently uncertain matters. We base our estimates and judgments on historical experiences and various other factors that we believe to be appropriate under the circumstances. Actual results may differ from these estimates, and we might obtain different estimates if we used different assumptions or factors. We had no significant changes in our critical accounting estimates since our last annual report. Our critical accounting estimates are identified and described in our annual report on Form 10-K for the year ended December 31, 2016.

### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

#### Commodity Price Risks

We are exposed to commodity price risks. Many of the ingredients we use to prepare our food, our packaging materials, as well as utilities to run our restaurants are commodities or ingredients that are affected by the price of other commodities, exchange rates, foreign demand, weather, seasonality, production, availability and other factors outside our control. We work closely with our suppliers and use a mix of forward pricing protocols under which we agree with our supplier on fixed prices for deliveries at some time in the future, fixed pricing protocols under which we agree on a fixed price with our supplier for the duration of that protocol, and formula pricing protocols under which the prices we pay are based on a specified formula related to the prices of the goods, such as spot prices. However, a majority of the dollar value of goods

## Table of Contents

purchased by us is effectively at spot prices. Generally, our pricing protocols with suppliers can remain in effect for periods ranging from one to 24 months, depending on the outlook for prices of the particular ingredient. In several cases, we have minimum purchase obligations. We have tried to increase, where necessary, the number of suppliers for our ingredients, which we believe can help mitigate pricing volatility. We follow industry news, trade issues, exchange rates, foreign demand, weather, crises and other world events that may affect our ingredient prices. Increases in ingredient prices could adversely affect our results if we choose for competitive or other reasons not to increase menu prices at the same rate at which ingredient costs increase, or if menu price increases result in customer resistance.

### Changing Interest Rates

We are also exposed to interest rate risk through fluctuations of interest rates on our investments. Changes in interest rates affect the interest income we earn, and therefore impact our cash flows and results of operations. As of September 30, 2017, we had \$475.4 million in investments and interest-bearing cash accounts, including insurance-related restricted trust accounts classified in other assets, and \$66.8 million in accounts with an earnings credit we classify as interest income, which combined earned a weighted-average interest rate of 0.87%.

### Foreign Currency Exchange Risk

A portion of our operations consists of activities outside of the U.S. and we have currency risk on the transactions in other currencies and translation adjustments resulting from the conversion of our international financial results into the U.S. dollar. However, a substantial majority of our operations and investment activities are transacted in the U.S. and therefore our foreign currency risk is not material at this date.

## ITEM 4.CONTROLS AND PROCEDURES

We maintain disclosure controls and procedures (as defined in Rule 13a-15(e) promulgated under the Securities Exchange Act of 1934, as amended (the “Exchange Act”)) that are designed to ensure that information required to be disclosed in Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission’s rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

As of September 30, 2017, we carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures. Based on the foregoing, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of the end of the period covered by this report.

There were no changes during the three months ended September 30, 2017, in our internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) that have materially affected or are reasonably likely to materially affect our internal control over financial reporting.

## PART II

### ITEM 1.LEGAL PROCEEDINGS



For information regarding legal proceedings, see Note 8. "Commitments and Contingencies" in our notes to the condensed consolidated financial statements included in Item 1. "Financial Statements".

#### ITEM 1A.RISK FACTORS

There have been no material changes in our risk factors since our annual report on Form 10-K for the year ended December 31, 2016, except as set forth below.

We may be harmed by security risks we face in connection with our electronic processing and transmission of confidential customer and employee information.

We accept electronic payment cards for payment in our restaurants. During 2016 approximately 70% of our sales were attributable to credit and debit card transactions, and credit and debit card usage could continue to increase. A number of retailers have experienced actual or potential security breaches in which credit and debit card information may have been stolen, including a number of highly publicized incidents with well-known retailers in recent years.

In April 2017, our information security team detected unauthorized activity on the network that supports payment processing for our restaurants, and immediately began an investigation with the help of leading computer security firms. We also self-reported the issue to payment card processors and law enforcement. Our investigation detected malware designed to access payment card data from cards used at point-of-sale

Table of Contents

devices at most Chipotle restaurants, primarily in the period from March 24, 2017 through April 18, 2017. We have removed the malware from our systems and continue to evaluate ways to enhance our security measures. However, we expect to be subject to payment card network assessments and may incur regulatory fines or penalties, for which our insurance coverage is limited, and as a result, we recorded a \$30 million estimated liability. We may ultimately be subject to liabilities greater than or less than the amount accrued. See Note 8. “Commitments and Contingencies” within Item 1. “Financial Statements,” for further discussion of potential liabilities and pending litigation filed against us in connection with this incident.

We may be subject to additional lawsuits or other proceedings in the future relating to the incident or any future incidents in which payment card data may have been compromised. Proceedings related to theft of credit or debit card information may be brought by payment card providers, banks and credit unions that issue cards, cardholders (either individually or as part of a class action lawsuit), or federal and state regulators. Any such proceedings could distract our management from running our business and cause us to incur significant unplanned losses and expenses. Consumer perception of our brand could also be negatively affected by these events, which could further adversely affect our results and prospects.

We are also required to collect and maintain personal information about our employees, and we collect information about customers as part of some of our marketing programs as well. The collection and use of such information is regulated at the federal and state levels, by the European Union and its member states, and the regulatory environment related to information security and privacy is increasingly demanding. At the same time, we are increasingly relying on cloud computing and other technologies that result in third parties holding significant amounts of customer or employee information on our behalf. We have seen an increase over the past several years in the frequency and sophistication of attempts to compromise the security of several of these systems. If the security and information systems that we or our outsourced third party providers use to store or process such information are compromised or if we, or such third parties, otherwise fail to comply with these laws and regulations, we could face litigation and the imposition of penalties that could adversely affect our financial performance. Our reputation as a brand or as an employer could also be adversely affected from these types of security breaches or regulatory violations, which could impair our sales or ability to attract and keep qualified employees.

## ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

## Purchases of Equity Securities by the Issuer

The table below reflects shares of common stock we repurchased during the third quarter of 2017.

|                                       | Total Number of<br>Shares Purchased | Average<br>Price<br>Paid Per<br>Share | Total Number of Shares Purchased as<br>Part of Publicly Announced Plans or<br>Programs(1) | Approximate<br>Dollar Value<br>of Shares that<br>May Yet Be<br>Purchased<br>Under the<br>Plans or<br>Programs(2) |
|---------------------------------------|-------------------------------------|---------------------------------------|---|--|
| July<br>Purchased 7/1<br>through 7/31 | 111,385                             | \$ 375.36                             | 111,385   | \$ 156,117,762   |

|           |                               |           |         |                |
|-----------|-------------------------------|-----------|---------|----------------|
| August    | 156,772                       | \$ 322.73 | 156,772 | \$ 105,521,981 |
|           | Purchased 8/1<br>through 8/31 |           |         |                |
| September | 32,405                        | \$ 311.59 | 32,405  | \$ 95,424,817  |
|           | Purchased 9/1<br>through 9/30 |           |         |                |
| Total     | 300,562                       | \$ 341.03 | 300,562 | \$ 95,424,817  |

(1) Shares were repurchased pursuant to repurchase programs announced on January 11, 2017 and May 23, 2017.

(2) This column does not include an additional \$100 million in authorized repurchases announced on October 24, 2017. Each repurchase program has no expiration date. Authorization of repurchase programs may be modified, suspended or discontinued at any time.

#### ITEM 3.DEFAULTS UPON SENIOR SECURITIES

None.

#### ITEM 4.MINE SAFETY DISCLOSURES

Not applicable.

#### ITEM 5.OTHER INFORMATION

None.

Table of Contents

## ITEM 6.EXHIBITS

## EXHIBIT INDEX

| Exhibit<br>Number | Exhibit Description  | Description of Exhibit Incorporated Herein by<br>Reference |           |                      |                   |                   |
|-------------------|--|--|-----------|----------------------|-------------------|-------------------|
|                   |  | Form   | File No.  | Filing<br>Date       | Exhibit<br>Number | Filed<br>Herewith |
| 3.1               | <u>Amended and Restated Certificate of Incorporation of Chipotle Mexican Grill, Inc.</u>   | 10-Q   | 001-32731 | October<br>26, 2016  | 3.1               |                   |
| 3.2               | <u>Chipotle Mexican Grill, Inc. Amended and Restated Bylaws</u>  | 8-K  | 001-32731 | October<br>6, 2016   | 3.1               |                   |
| 4.1               | <u>Form of Stock Certificate for Shares of Common Stock</u>  | 10-K   | 001-32731 | February<br>10, 2012 | 4.1               |                   |
| 31.1              | <u>Certification of Chief Executive Officer of Chipotle Mexican Grill, Inc. pursuant to Section 302 of the Sarbanes-Oxley Act of 2002</u>  | -  | -         | -                    | -                 | X                 |
| 31.2              | <u>Certification of Chief Financial Officer of Chipotle Mexican Grill, Inc. pursuant to Section 302 of the Sarbanes-Oxley Act of 2002</u>  | -  | -         | -                    | -                 | X                 |
| 32.1              | <u>Certification of Chief Executive Officer and Chief Financial Officer of Chipotle Mexican Grill, Inc. pursuant to Section 906 of the Sarbanes-Oxley Act of 2002</u>  | -  | -         | -                    | -                 | X                 |
| 101               | The following financial statements, formatted in XBRL: (i) Condensed Consolidated Balance Sheet as of September 30, 2017 and December 31, 2016, (ii) Condensed Consolidated Statement of Income for the three and nine months ended September 30, 2017 and 2016, (iii) Condensed Consolidated Statement of Comprehensive Income for the three and nine months ended September 30, 2017 and 2016, (iv) Condensed Consolidated Statement of Cash Flows for the nine months ended September 30, 2017 and 2016; and (v) Notes to the Condensed Consolidated Financial Statements | -  | -         | -                    | -                 | X                 |



Table of Contents

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.

CHIPOTLE MEXICAN GRILL, INC.

By: /S/ JOHN R. HARTUNG

Name: John R. Hartung  
Title: Chief Financial Officer (principal financial officer and duly authorized signatory for the registrant)

Date: October 24, 2017