STEVEN MADDEN, LTD.
Form 10-Q
November 09, 2010

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2010

or

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

For the transition period from _________________ to _____________________

Commission File Number 0-23702

STEVEN MADDEN, LTD.
(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	13-3588231 (I.R.S. Employer Identification No.)
52-16 Barnett Avenue, Long Island City, New York (Address of principal executive offices)	11104 (Zip Code)

Registrant’s telephone number, including area code (718) 446-1800

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

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

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

Large accelerated filer o	Accelerated filer x
Non-accelerated filer o (do not check if smaller reporting company)	Smaller reporting company o

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

As of November 5, 2010, the latest practicable date, there were 27,742,346 shares of common stock, $.0001 par value, outstanding.

STEVEN MADDEN, LTD.
FORM 10-Q
QUARTERLY REPORT
September 30, 2010

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PART I. FINANCIAL INFORMATION
Item 1. Condensed Consolidated Financial Statements
STEVEN MADDEN, LTD. AND SUBSIDIARIES

Condensed Consolidated Balance Sheets
(in thousands)

	September 30, 2010 (unaudited)	December 31, 2009	September 30, 2009 (unaudited)
ASSETS			
Current assets:			
Cash and cash equivalents	$ 29,045	$ 69,266	$ 47,622
Accounts receivable, net of allowances of $2,209, $1,195 and $1,806	12,846	11,071	9,909
Due from factors, net of allowances of $10,934, $12,487 and $9,789	81,815	47,534	67,884
Inventories	44,485	30,453	29,678
Marketable securities – available for sale	20,395	17,971	12,815
Prepaid expenses and other current assets	11,590	6,295	6,896
Deferred taxes	8,827	8,779	7,746
Total current assets	209,003	191,369	182,550
Notes receivable	33,195	—	—
Note receivable – related party	3,791	3,568	3,552
Property and equipment, net	21,054	23,793	24,750
Deferred income taxes	6,309	7,543	6,688
Deposits and other	2,775	1,844	1,992
Marketable securities – available for sale	103,179	67,713	65,254
Goodwill – net	36,613	24,313	24,313
Intangibles – net	14,095	6,716	7,191
Total Assets	$ 430,014	$ 326,859	$ 316,290
LIABILITIES			
Current liabilities:			
Accounts payable	$ 37,302	$ 24,544	$ 26,682
Accrued expenses	21,525	15,338	16,914
Income taxes payable	5,935	166	8,729
Accrued incentive compensation	11,864	12,314	8,819
Total current liabilities	76,626	52,362	61,144
Contingent payment liability	12,000	—	—
Deferred rent	5,494	5,044	4,974
Other liabilities	1,577	1,666	274
Total Liabilities	95,697	59,072	66,392

Commitments, contingencies and other						
STOCKHOLDERS' EQUITY						
Preferred stock – $.0001 par value, 5,000 shares authorized; none issued; Series A Junior Participating preferred stock – $.0001 par value, 60 shares authorized; none issued						
Common stock – $.0001 par value, 60,000 shares authorized, 36,122 35,687 and 35,438 shares issued, 27,719, 27,425 and 27,176 outstanding		4		3		3
Additional paid-in capital		158,945		147,703		143,437
Retained earnings		305,465		247,365		233,809
Other comprehensive income:						
Unrealized gain on marketable securities		2,446		700		633
Treasury stock – 8,403, 8,262 and 8,262 shares at cost		(132,543)		(127,984)		(127,984)
Total Stockholders' Equity		334,317		267,787		249,898
Total Liabilities and Stockholders' Equity	$	430,014	$	326,859	$	316,290

See accompanying notes to condensed consolidated financial statements - unaudited

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STEVEN MADDEN, LTD. AND SUBSIDIARIES

Condensed Consolidated Statements of Income
(unaudited)
(in thousands, except per share data)

	Three Months Ended September 30, 2010	Three Months Ended September 30, 2009	Nine Months Ended September 30, 2010	Nine Months Ended September 30, 2009
Net sales	$184,118	$ 140,138	$474,390	$ 364,039
Cost of sales	106,610	78,462	268,096	209,313
Gross profit	77,508	61,676	206,294	154,726
Commission, royalty and licensing fee income – net	6,587	5,726	18,000	15,993
Operating expenses	(46,707)	(39,088)	(129,994)	(112,729)
Income from operations	37,388	28,314	94,300	57,990
Interest and other income, net	1,201	488	2,927	1,252
Income before provision for income taxes	38,589	28,802	97,227	59,242
Provision for income taxes	15,673	10,971	39,127	22,690
Net income	$22,916	$ 17,831	$58,100	$ 36,552
Basic income per share	$0.83	$ 0.66	$2.11	$ 1.35
Diluted income per share	$0.81	$ 0.64	$2.06	$ 1.34
Basic weighted average common shares outstanding	27,680	27,152	27,593	27,003
Effect of dilutive securities – options/restricted stock	555	522	643	356
Diluted weighted average common shares outstanding	28,235	27,674	28,236	27,359

See accompanying notes to condensed consolidated financial statements - unaudited

STEVEN MADDEN, LTD. AND SUBSIDIARIES

Condensed Consolidated Statements of Cash Flows
(unaudited)
(in thousands)

	Nine Months Ended September 30,	
	2010	2009
Cash flows from operating activities:		
Net income	$58,100	$36,552
Adjustments to reconcile net income to net cash provided by operating activities:		
Excess tax benefit from the exercise of options	(2,882)	(187)
Depreciation and amortization	7,364	7,113
Loss on disposal of fixed assets	543	718
Non-cash compensation	5,963	4,332
Provision for bad debts	(539)	294
Accrued interest on note receivable – related party	(223)	(182)
Deferred rent expense	463	169
Realized (gain) loss on marketable securities	(32)	65
Changes in:		
Accounts receivable	(2,121)	(4,618)
Due from factor	(32,728)	(33,591)
Inventories	(13,732)	1,919
Prepaid expenses, deposits and other assets	(4,216)	1,086
Accounts payable and other accrued expenses	26,534	23,773
Other liabilities	(102)	(1,019)
Net cash provided by operating activities	42,392	36,424
Cash flows from investing activities:		
Purchase of property and equipment	(2,280)	(2,403)
Purchase of marketable securities	(54,341)	(54,699)
Sale/redemption of marketable securities	18,592	12,913
Purchase of notes receivable	(34,186)	—
Acquisitions, net of cash acquired *	(11,119)	(5,776)
Net cash used in investing activities	(83,334)	(49,965)
Cash flows from financing activities:		
Repayment of advances from factor	—	(30,168)
Proceeds from options exercised	2,398	1,556
Tax benefit from exercise of options	2,882	187
Purchase of common stock for treasury	(4,559)	—
Net cash provided by (used in) financing activities	721	(28,425)
Net decrease in cash and cash equivalents	(40,221)	(41,966)

Cash and cash equivalents – beginning of period	69,266	89,588
Cash and cash equivalents – end of period	$29,045	$47,622

* The amount for 2009 includes $4,526 which was accrued at December 31, 2008.

See accompanying notes to condensed consolidated financial statements - unaudited

STEVEN MADDEN, LTD. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements – Unaudited
September 30, 2010
($ in thousands except share and per share data)

Note A – Basis of Reporting

The accompanying unaudited condensed consolidated financial statements of Steven Madden, Ltd. and subsidiaries (the "Company") have been prepared in accordance with the generally accepted accounting principles in the United States of America ("GAAP") for interim financial information and pursuant to the rules and regulations of the Securities and Exchange Commission (the "SEC"). Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, such statements include all adjustments (consisting only of normal recurring items) which are considered necessary for a fair presentation of the financial position of the Company and the results of its operations and cash flows for the periods presented. The results of its operations for the three- and nine-month periods ended September 30, 2010 are not necessarily indicative of the operating results for the full year. It is suggested that these financial statements be read in conjunction with the financial statements and related disclosures for the year ended December 31, 2009 included in the Annual Report of Steven Madden, Ltd. on Form 10-K filed with the SEC on March 12, 2010.

Note B – Stock Split

On March 24, 2010, the Board of Directors declared a 3-for-2 stock split of the Company's outstanding shares of common stock, effected in the form of a stock dividend on the Company's outstanding common stock. Stockholders of record at the close of business on April 20, 2010 received one additional share of Steven Madden, Ltd. common stock for every two shares of common stock owned on that date. The additional shares were distributed on May 3, 2010. Stockholders received cash in lieu of any fractional shares of common stock they otherwise would have received in connection with the dividend. All share and per share data provided herein gives effect to this stock split, applied retroactively.

Note C – Recently Adopted Accounting Standards

In January 2010, the Financial Accounting Standards Board ("FASB") issued new accounting guidance which expands disclosure requirements relating to fair value measurements. The guidance adds requirements for disclosing amounts of and reasons for significant transfers into and out of Levels 1 and 2 and requires gross rather than net disclosures about purchases, sales, issuance and settlements relating to Level 3 measurements. The guidance also provides clarification that fair value measurement disclosures are required for each class of assets and liabilities. Disclosures about the valuation techniques and inputs used to measure fair value for measurements that fall in either Level 2 or Level 3 are also required. The Company adopted the provisions of the guidance as of March 31, 2010, except for disclosure about purchases, sales, issuance and settlements in the roll forward of activity in Level 3 fair value measurement, which is effective for fiscal years beginning after December 15, 2010. Disclosures are not required for earlier periods presented for comparative purposes. The new guidance affects disclosures only and, therefore, the adoption had no impact on the Company's results of operation or financial position.

A new accounting pronouncement amending the consolidation guidance relating to variable interest entities ("VIE") became effective for the Company on January 1, 2010. The new guidance replaces the current quantitative model for determining the primary beneficiary of a VIE with a qualitative approach that considers which entity has the power to direct activities that most significantly impact the VIE's performance and whether the entity has an obligation to absorb losses or the right to receive benefits that could potentially be significant to the VIE. The adoption of the

accounting pronouncement had no material impact on the Company's Condensed Consolidated Financial Statements.

Note D – Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

STEVEN MADDEN, LTD. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements – Unaudited
September 30, 2010
($ in thousands except share and per share data)

Note D – Use of Estimates (continued)

Significant areas involving management estimates include allowances for bad debts, returns and customer chargebacks, and deferred tax asset valuation allowance. The Company provides reserves on trade accounts receivable and due from factors for future customer chargebacks and markdown allowances, discounts, returns and other miscellaneous compliance related deductions that relate to the current period sales. The Company evaluates anticipated chargebacks by reviewing several performance indicators of its major customers. These performance indicators, which include retailers' inventory levels, sell-through rates and gross margin levels, are analyzed by management to estimate the amount of the anticipated customer allowance.

Note E – Due To and From Factor

The Company has a collection agency agreement with Rosenthal & Rosenthal, Inc. ("Rosenthal"). Under the agreement, the Company can request advances from Rosenthal of up to 85% of aggregate receivables factored by Rosenthal. The agreement provides the Company with a credit facility in the amount of $30,000, having a sub-limit of $15,000 on the aggregate face amount of letters of credit, at an interest rate that, at the Company's election, is tied to either the prime rate or LIBOR.

Note F – Notes Receivable

As of September 30, 2010, Notes Receivable were comprised of the following:

Due from Bakers Footwear Group, Inc.	$4,009
Due from Betsey Johnson LLC	29,186
Total	$33,195

On August 26, 2010, the Company entered into a Debenture and Stock Purchase Agreement with Bakers Footwear Group, Inc. ("Bakers") pursuant to which the Company paid $5,000 to acquire a subordinated debenture in the principal amount of $5,000 and 1,844,860 unregistered shares of Bakers common stock which trades on the Over-the-Counter Bulletin Board. The Company allocated $996 of the purchase price to the common stock and $4,004 to the subordinated debenture. The debenture, which has an interest rate of 11% payable quarterly in cash, is payable in four equal installments of $1,250 due on August 31, 2017, 2018, 2019 and 2020. The difference between the $4,004 purchase price of the debenture and the $5,000 principal amount of the debenture is considered original issue discount and is being amortized over the life of the debenture. As of September 30, 2010, the total amount of the discount amortized was $5 bringing the value of the note to $4,009.

On August 27, 2010, the Company purchased from various members of a loan syndicate their respective participations in a term loan in the aggregate outstanding principal amount of $48,750 (the "Loan") made by the syndicate lenders to Betsey Johnson LLC ("Betsey Johnson"). The Loan was originally made to Betsey Johnson pursuant to a Loan and Security Agreement dated as of August 20, 2007 (the "Syndicate Loan Agreement") between Betsey Johnson and the syndicate lenders, which provided Betsey Johnson a term loan of $50,000. The Syndicate Loan Agreement contemplated repayment of principal in quarterly installments of varying amounts over the course of the loan with a final installment on August 20, 2012 and interest accruing at a rate equal to the greater of 10% or LIBOR plus

5%. The Loan, which was secured by a first priority security interest on substantially all assets of Betsey Johnson, was in default on the date of purchase. The aggregate purchase price paid by the Company to the syndicate lenders for their participations in the Loan was $29,186, including transaction costs. On October 5, 2010, the Company entered into a Restructuring Agreement with Betsey Johnson to effect a restructuring of the Loan. See Note S for a description of the restructuring of the Loan. In addition, on October 5, 2010, the Company made a new secured term loan to Betsey Johnson in the principal amount of $3,000 at an interest rate of 8% per annum. The principal amount and all accrued interest on the term loan will become due on December 31, 2015. The term loan is secured by a first priority security interest on substantially all of the remaining properties and assets of Betsey Johnson.

STEVEN MADDEN, LTD. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements – Unaudited
September 30, 2010
($ in thousands except share and per share data)

Note G – Note Receivable – Related Party

On June 25, 2007, the Company made a loan to Steve Madden, its Creative and Design Chief and a principal stockholder of the Company, in the amount of $3,000, in order for Mr. Madden to satisfy a personal tax obligation resulting from the exercise of options that were due to expire and retain the underlying Company common stock, which he pledged to the Company as collateral to secure the loan. Mr. Madden executed a secured promissory note in favor of the Company bearing interest at an annual rate of 8% which was due on the earlier of the date Mr. Madden ceases to be employed by the Company or December 31, 2007. An amendment to the note dated December 19, 2007 extended the due date to March 31, 2009, and a second amendment dated April 1, 2009 changed the interest rate to 6% and extended the due date of both principal and interest to June 30, 2015. As of September 30, 2010, $791 of interest has accrued on the note and has been reflected on the Company's Condensed Consolidated Financial Statements. Due to the 3-for-2 stock split effected on May 3, 2010 (see Note B above) the number of shares securing the loan increased from 510,000 shares to 765,000 shares. Based upon the increase in the market value of the Company's common stock since the inception of the loan, on July 12, 2010, the Company determined to release from its security interest 555,000 shares of the Company's common stock, retaining 210,000 shares with a total market value on that date of $6,798, as collateral for the loan.

Note H – Marketable Securities

Marketable securities consist primarily of corporate and U.S. government and federal agency bonds with maturities greater than three months and up to six years at the time of purchase. These securities, which are classified as available-for-sale, are carried at fair value, with unrealized gains and losses, net of any tax effect, reported in stockholders' equity as accumulated other comprehensive income (loss). These securities are classified as current and non-current marketable securities based upon their maturities. Amortization of premiums and discounts is included in interest income. For the three- and nine-month periods ended September 30, 2010, the amortization of bond premiums totals $320 and $822, respectively, compared to $396 and $563 for the comparable periods in 2009. The values of these securities may fluctuate as a result of changes in market interest rates and credit risk.

Note I – Fair Value Measurement

The Company adopted the provisions of FASB ASC 820-10, "Fair Value Measurements and Disclosures" ("ASC 820-10") for financial assets and liabilities effective January 1, 2008, and adopted ASC 820-10 for non-financial assets and non-financial liabilities effective January 1, 2009. ASC 820-10 clarifies the principle that fair value should be based on the assumptions market participants would use when pricing an asset or liability and establishes a fair value hierarchy that prioritizes the information used to develop those assumptions. ASC 820-10 utilizes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into three broad levels.

A brief description of those three levels is as follows:

Level 1: Observable inputs such as quoted prices in active markets for identical assets or liabilities.
Level 2: Inputs other than quoted prices that are observable for the asset or liability, either directly or indirectly.
Level 3: Significant unobservable inputs.

STEVEN MADDEN, LTD. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements – Unaudited
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($ in thousands except share and per share data)

Note I – Fair Value Measurement (continued)

The Company's financial assets subject to fair value measurements as of September 30, 2010 are as follows:

		Fair Value Measurements Using Fair Value Hierarchy		
	Fair value	Level 1	Level 2	Level 3
Assets:				
Cash equivalents	$1,047	$1,047	$—	$—
Current marketable securities – available for sale	20,395	20,395	—	—
Investment in Bakers	996	—	996	—
Note receivable – Bakers	4,009	—	—	4,009
Note receivable – Betsey Johnson	29,186	—	—	29,186
Long-term marketable securities – available for sale	103,179	103,179	—	—
Total assets	$158,812	$124,621	$996	$33,195
Liabilities:				
Contingent consideration	$12,000	—	—	$12,000
Total liabilities	$12,000	—	—	$12,000

The Company's financial assets subject to fair value measurements as of December 31, 2009 are as follows:

		Fair Value Measurements Using Fair Value Hierarchy		
	Fair value	Level 1	Level 2	Level 3
Cash equivalents	$30,962	$30,962	—	—
Current marketable securities – available for sale	17,971	17,971	—	—
Long-term marketable securities – available for sale	67,713	67,713	—	—
Total	$116,646	$116,646	—	—

Pursuant to the Debenture and Stock Purchase Agreement with Bakers (see Note F), the Company received 1,844,860 unregistered shares of Bakers common stock, which trades on the OTC Bulletin Board. These shares, which are thinly traded, were valued using the quoted price of similar registered shares of Bakers common stock adjusted for the effect of the transfer restriction, considering factors such as the nature and duration of the transfer restriction, the volatility of the stock and the risk free interest rate. The shares are included in deposits and other assets on the Company's Condensed Consolidated Balance Sheet. For the note receivable due from Bakers (see note F), which was purchased at a substantial discount, the carrying value was determined to be the fair value. The note receivable due from Betsey Johnson (see Note F), which was in default on the date of purchase, was valued using the estimated fair value of the

collateral. On October 5, 2010, the Company entered into a Restructuring Agreement with Betsey Johnson to effect a restructuring of the Loan. See Note S for a description of the restructuring of the Loan. No gains or losses resulting from the fair value measurement of financial assets were included in the Company's earnings. The Company has recorded a liability for contingent consideration as a result of the February 10, 2010 acquisition of Big Buddha, Inc. (see Note S). The contingent consideration may be paid to the seller of Big Buddha based on the financial performance of Big Buddha for each of the twelve-month periods ending on March 31, 2011, 2012 and 2013. The fair value of the contingent payments was estimated using the present value of management's projections of the financial results of Big Buddha during the earn-out period.

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STEVEN MADDEN, LTD. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements – Unaudited
September 30, 2010
($ in thousands except share and per share data)

Note I – Fair Value Measurement (continued)

In April 2009, the FASB issued additional guidance for estimating fair value in accordance with ASC Topic 820. The additional guidance addresses determining fair value when the volume and level of activity for an asset or liability have significantly decreased and identifying transactions that are not orderly. The adoption of this guidance did not have a material effect on the Company's Condensed Consolidated Financial Statements.

The Company adopted the provisions of FASB ASC 825-10, "Financial Instruments" ("ASC 825-10") on January 1, 2008. ASC 825-10 permits entities to choose to measure many financial instruments and certain other items at fair value that are not currently required to be measured at fair value. ASC 825-10 also establishes presentation and disclosure requirements designed to facilitate comparisons between entities that chose different measurement attributes for similar assets and liabilities. The Company has elected not to measure any eligible items at fair value.

Note J – Fair Value of Financial Instruments

The carrying value of certain financial instruments such as accounts receivable, due from factors and accounts payable approximate their fair values due to their short-term nature of their underlying terms. The fair values of the financial instruments and investments are determined by reference to market data and other valuation techniques, as appropriate. Fair value of the note receivable – related party approximates its carrying value based upon its interest rate, which approximates current market interest rates.

Note K – Inventories

Inventories, which consist of finished goods on hand and in transit, are stated at the lower of cost (first-in, first-out method) or market.

Note L – Revenue Recognition

The Company recognizes revenue on wholesale sales when products are shipped pursuant to its standard terms which are freight on board ("FOB") warehouse or when products are delivered to the consolidators as per the terms of the customers' purchase order. Sales reductions for anticipated discounts, allowances and other deductions are recognized during the period when sales are recorded. Customers retain the right to replacement of the product for poor quality or improper or short shipments, which have historically been immaterial. Retail sales are recognized when the payment is received from customers and are recorded net of returns. The Company also generates commission income acting as a buying agent by arranging to manufacture private label shoes to the specifications of its clients. The Company's commission revenue includes partial recovery of its design, product and development costs for the services provided to certain suppliers in connection with the Company's private label business. Commission revenue and product and development cost recoveries are recognized as earned when title to the product transfers from the manufacturer to the customer and collections are reasonably assured and are reported on a net basis after deducting related operating expenses.

The Company licenses its trademarks for use in connection with the manufacturing, marketing and sale of cold weather accessories, sunglasses, eyewear, outerwear, bedding hosiery, women's fashion apparel and jewelry. The

license agreements require the licensee to pay the Company a royalty and, in substantially all of the agreements, an advertising fee based on the higher of a minimum or a net sales percentage as defined in the various agreements. In addition, under the terms of retail selling agreements, most of the Company's international distributors are required to pay the Company a royalty based on a percentage of net sales, in addition to a commission on the purchases of the Company's products. Licensing revenue is recognized on the basis of net sales reported by the licensees and international distributors, or the minimum guaranteed royalties, if higher. In substantially all of the Company's license agreements, the minimum guaranteed royalty is earned and payable on a quarterly basis.

STEVEN MADDEN, LTD. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements – Unaudited
September 30, 2010
($ in thousands except share and per share data)

Note M – Taxes Collected From Customers

The Company accounts for certain taxes collected from its customers in accordance with the accounting guidance which permits companies to adopt a policy of presenting taxes in the income statement on either a gross basis (included in revenues and costs) or net basis (excluded from revenues). Taxes within the scope of the accounting guidance would include taxes that are imposed on a revenue transaction between a seller and a customer, for example, sales taxes, use taxes, value-added taxes and some types of excise taxes. The Company has consistently recorded all taxes on a net basis.

Note N – Sales Deductions

The Company supports retailers' initiatives to maximize the sales of its products on the retail floor by subsidizing the co-op advertising programs of such retailers, providing them with inventory markdown allowances and participating in various other marketing initiatives of its major customers. In addition, the Company accepts returns for damaged product which is charged back to the responsible factory. Such expenses are reflected in the Condensed Consolidated Statement of Income as deductions to sales. For the three- and nine-month periods ended September 30, 2010, the deduction to sales for these expenses as a total dollar amount and as a percentage of gross sales was $10,331 or 6.3% and $25,515 or 6.2%, respectively, as compared to $6,593 or 5.6% and $20,185 or 6.7% for the comparable periods in 2009.

Note O – Cost of Sales

All costs incurred to bring finished products to the Company's distribution center and, in the Retail segment, the costs to bring products to the Company's stores, are included in the cost of sales line on the Condensed Consolidated Statement of Income. These include the cost of finished products, purchase commissions, letter of credit fees, brokerage fees, sample expenses, custom duty, inbound freight, royalty payments on licensed products, labels and product packaging. All warehouse and distribution costs related to the Wholesale segments and freight to customers, if any, are included in the operating expenses line item of the Company's Condensed Consolidated Statement of Income. The Company's gross margins may not be comparable to those of other companies in the industry because some companies may include warehouse and distribution costs, as well as other costs excluded from cost of sales by the Company, as a component of cost of sales, while other companies report on the same basis as the Company and include them in operating expenses.

Note P – Income Taxes

The Company's effective income tax rate for the nine months ended September 30, 2010 and 2009 was 40.2% and 38.3%, respectively. The increase in the effective income tax rate is substantially attributable to increases in state and local taxes, among other matters, including revisions of allocation formulas by some tax jurisdictions resulting in the Company having higher taxable income in those jurisdictions.

Note Q – Net Income Per Share of Common Stock

Basic income per share is based on the weighted average number of shares of common stock outstanding during the period. Diluted income per share reflects: (a) the potential dilution assuming shares of common stock were issued upon the exercise of outstanding in-the-money options and the proceeds thereof were used to purchase treasury stock at the average market price during the period, and (b) the vesting of granted nonvested restricted stock awards for which the assumed proceeds upon grant are deemed to be the amount of compensation cost attributable to future services and are not yet recognized using the treasury stock method, to the extent dilutive. For both the three- and nine-month periods ended September 30, 2010, options to purchase 177,100 shares of the Company’s common stock have been excluded from the calculation because inclusion of such shares would be anti-dilutive as compared with options to purchase 32,000 and 136,000 shares of the Company’s common stock that have been excluded from the calculation for the three and nine months ended September 30, 2009.

STEVEN MADDEN, LTD. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements – Unaudited
September 30, 2010
($ in thousands except share and per share data)

Note R – Stock-Based Compensation

In March 2006, the Board of Directors approved the Steven Madden, Ltd. 2006 Stock Incentive Plan (the "Plan") under which nonqualified stock options, stock appreciation rights, performance shares, restricted stock, other stock-based awards and performance-based cash awards may be granted to employees, consultants and non-employee directors. The stockholders approved the Plan on May 26, 2006. On May 25, 2007, the stockholders approved an amendment to the Plan to increase the maximum number of shares that may be issued under the Plan from 1,800,000 to 2,325,000. On May 22, 2009, the stockholders approved a second amendment to the Plan that increased the maximum number of shares that may be issued under the Plan to 6,096,000. The following table summarizes the number of shares of common stock authorized for issuance under the Plan, the amount of stock-based awards issued (net of expired or cancelled) under the Plan and the number of shares of common stock available for the grant of stock-based awards under the Plan:

Common Stock authorized	6,096,000
Stock based awards, including restricted stock and stock options granted, net of expired or cancelled	3,460,000
Common Stock available for grant of stock based awards as of September 30, 2010	2,636,000

Total equity-based compensation for the three and nine months ended September 30 is as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Restricted stock	$ 1,110	$ 1,087	$ 3,440	$ 3,268
Stock options	1,177	472	2,523	1,064
Total	$ 2,287	$ 1,559	$ 5,963	$ 4,332

Equity-based compensation is included in operating expenses on the Company's Condensed Consolidated Statements of Income.

Stock Options

Cash proceeds and intrinsic values related to total stock options exercised during both the three- and nine-month periods ended September 30, 2010 and 2009 are as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
	$ 485	$ 345	$ 2,398	$ 1,556

Proceeds from stock options exercised				
Intrinsic value of stock options exercised	$ 808	$ 396	$ 5,422	$ 1,557

During the three and nine months ended September 30, 2010, approximately 51,000 and 316,000 options vested with a weighted average exercise price of $22.46 and $15.40, respectively. During the three and nine months ended September 30, 2009, 21,000 and 120,000 options vested with a weighted average exercise price of $12.10 and $12.18, respectively. As of September 30, 2010, there were 1,559,000 unvested options with a total of $10,752 of unrecognized compensation cost and a weighted average vesting period of 3.1 years. As of September 30, 2009, there were 1,241,000 unvested options with a total of $5,376 of unrecognized compensation cost and a weighted average vesting period of 3.4 years.

STEVEN MADDEN, LTD. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements – Unaudited
September 30, 2010
($ in thousands except share and per share data)

Note R – Stock-Based Compensation (continued)

The Company estimates the fair value of options granted using the Black-Scholes option-pricing model, which requires several assumptions. The expected term of the options represents the estimated period of time until exercise and is based on the historical experience of similar awards. Expected volatility is based on the historical volatility of the Company's common stock. The risk free interest rate is based on the U.S. Treasury yield curve in effect at the time of the grant. With the exception of a special dividend paid in November of 2005 and 2006, the Company historically has not paid dividends and thus the expected dividend rate is assumed to be zero. The following weighted average assumptions were used for stock options granted:

	Nine Months Ended September 30,	
	2010	2009
Expected volatility	47.2% to 52.4%	49.2% to 52.1%
Risk-free interest rate	1.08% to 2.16%	1.39% to 2.09%
Expected life (in years)	2.8 to 4.4	3.4 to 3.9
Expected dividend yield	None	None
Weighted average fair value	$ 12.68	$ 5.78

Activity relating to stock options granted under the Company's plans during the nine months ended September 30, 2010 is as follows:

	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value
Outstanding at January 1, 2010	1,615,000	$ 13.68		
Granted	621,000	33.40		
Exercised	(231,000)	10.81		
Cancelled/Forfeited	(26,000)	22.56		
Outstanding at September 30, 2010	1,980,000	$ 20.09	5.3	$ 41,512
Exercisable at September 30, 2010	421,000	$ 13.19	4.1	$ 11,721

STEVEN MADDEN, LTD. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements – Unaudited
September 30, 2010
($ in thousands except share and per share data)

Note R – Stock-Based Compensation (continued)

Restricted Stock

The following table summarizes restricted stock activity during the nine months ended September 30, 2010 and 2009:

	2010		2009	
	Number of Shares	Weighted Average Fair Value at Grant Date	Number of Shares	Weighted Average Fair Value at Grant Date
Non-vested at January 1	447,000	$ 20.97	358,000	$ 29.53
Granted	118,000	30.50	23,000	22.19
Vested	(191,000)	20.02	(131,000)	29.58
Forfeited	(10,000)	28.49	(1,000)	34.05
Non-vested at September 30	363,000	$ 22.01	249,000	$ 28.79

As of September 30, 2010, there was $6,046 of total unrecognized compensation cost related to restricted stock awards granted under the Plan. This cost is expected to be recognized over a weighted average of 2.4 years. The Company determines the fair value of its restricted stock awards based on the market price of its common stock on the date of grant.

Note S – Acquisitions

Betsey Johnson intellectual property

On October 5, 2010, the Company acquired from Betsey Johnson, among other things, the Betsey Johnson® and Betseyville® trademarks through a series of transactions. First, on August 27, 2010, the Company purchased from various members of a loan syndicate their respective participations in a term loan in the aggregate outstanding principal amount of $48,750 (the "Loan") made by the syndicate lenders to Betsey Johnson. The aggregate purchase price paid by the Company to the syndicate lenders for their participation in the Loan was $29,186, including transaction costs. The Loan was in default on the date of purchase. See Notes F and I for additional disclosure on the Loan. Then, on October 5, 2010, the Company entered into a Restructuring Agreement with Betsey Johnson to effect a restructuring of the Loan. Pursuant to the Restructuring Agreement, in consideration of the elimination of the total amounts owed under the Loan, the Company acquired (a) substantially all trademarks, brand names, logos, business names, patents, copyrights and other intellectual property, including the right to receive royalties and other income with respect to the Betsey Johnson® and related marks and brands, (b) certain intellectual property licenses and other contracts of Betsey Johnson (c) a lease for an outlet store located in Riverhead, NY, and (d) a number of Class B Preferred Shares of Betsey Johnson constituting 10% of the issued and outstanding shares of Betsey Johnson. The total purchase price of $29,186, which is currently included in the notes receivable line of the Company's Condensed Consolidated Balance Sheets, will be allocated to the various acquired assets upon the completion of the Company's valuation of the fair value of these assets. Prior to its entry into the Restructuring Agreement with Betsey Johnson, the

Company had licensed from Betsey Johnson the right to use the Betsey Johnson® and Betseyville® trademarks in connection with the sale and marketing of handbags, small leather goods, belts and umbrellas.

STEVEN MADDEN, LTD. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements – Unaudited
September 30, 2010
($ in thousands except share and per share data)

Note S – Acquisitions (continued)

Big Buddha

On February 10, 2010, the Company acquired all of the outstanding shares of stock of privately held Big Buddha, Inc. ("Big Buddha") from its sole stockholder ("Seller"). Founded in 2003, Big Buddha designs and markets fashion-forward handbags to specialty retailers and better department stores. Management believes that Big Buddha is a strategic fit for the Company. The acquisition was completed for consideration of $11,119 in cash, net of cash acquired, plus contingent payments pursuant to an earn-out agreement with the Seller. The earn-out agreement provides for potential payments to the Seller based on the financial performance of Big Buddha handbags for each of the twelve-month periods ending on March 31, 2011, 2012 and 2013. The fair value of the contingent payments was estimated using the present value of management's projections of the financial results of Big Buddha during the earn-out period. As of September 30, 2010, the Company estimates the fair value of the contingent consideration to be $12,000.

The transaction was accounted for using the acquisition method required by GAAP. Accordingly, the assets and liabilities of Big Buddha were adjusted to their fair values, and the excess of the purchase price over the fair value of the assets acquired, including identified intangible assets, was recorded as goodwill. The fair values assigned to tangible and intangible assets acquired and liabilities assumed are based on management's estimates and assumptions, which are subject to change. The purchase price has been preliminarily allocated as follows:

Accounts receivable	$ 668
Inventory	1,212
Prepaid expenses and other current assets	102
Trade name	4,100
Customer relationships	4,900
Non-compete agreement	450
Accounts payable	(171)
Accrued expenses	(442)
Total fair value excluding goodwill	10,819
Goodwill	12,300
Net assets acquired	$ 23,119

The purchase price and related allocation are preliminary and may be revised as a result of adjustments made to the purchase price as additional information regarding assets and liabilities require. Contingent consideration classified as a liability will be remeasured at fair value at each reporting date, until the contingency is resolved, with changes recognized in earnings. The goodwill related to this transaction is expected to be deductible for tax purposes over 15 years.

The Company incurred approximately $430 in acquisition related costs applicable to the Big Buddha transaction during the nine months ended September 30, 2010. These expenses are included in operating expenses in the Company's Condensed Consolidated Statements of Income.

The results of operations of Big Buddha have been included in the Company's Condensed Consolidated Statements of Income from the date of the acquisition. Unaudited pro forma information related to this acquisition is not included, as the impact of this transaction is not material to the Company's consolidated results.

STEVEN MADDEN, LTD. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements – Unaudited
September 30, 2010
($ in thousands except share and per share data)

Note S – Acquisitions (continued)

Zone 88 and Shakedown Street

On July 8, 2009, the Company acquired certain of the assets constituting the Zone 88 and Shakedown Street (together "Zone 88") lines of SML Brands, LLC, a subsidiary of Aimee Lynn, Inc. SML Brands designs, sources and markets primarily private label accessories and licensed brands, principally handbags, belts and small leather goods, for mass merchants and mid-tier retailers. The acquisition was completed for $1,348 in cash. The fair values assigned to tangible and intangible assets acquired and liabilities assumed are based on management's estimates. The Company allocated $220 to current assets, $409 to the value of customer relationships, $841 to goodwill and $122 to liabilities assumed. The value of customer relationships is being amortized over ten years. The results of operations of Zone 88 have been included in the Company's Condensed Consolidated Statements of Income from the date of the acquisition. Unaudited pro forma information related to this acquisition is not included, as the impact of this transaction is not material to the Company's consolidated results.

Note T – Goodwill and Intangible Assets

The following is a summary of the carrying amount of goodwill by segment for the nine months ended September 30, 2010:

	Wholesale			Net Carrying
	Footwear	Accessories	Retail	Amount
Balance at January 1, 2010	$1,547	$17,265	$5,501	$24,313
Acquisition of Big Buddha	0	12,300	0	12,300
Balance at September 30, 2010	$1,547	$29,565	$5,501	$36,613

The following table details identifiable intangible assets as of September 30, 2010:

	Estimated Lives	Cost Basis	Accumulated Amortization	Net Carrying Amount
Trade name	6–10 years	$ 4,300	$ 432	$ 3,868
Customer relationships	10 years	11,709	2,871	8,838
License agreements	3–6 years	5,600	4,833	767
Non-compete agreement	5 years	1,380	758	622
Other	3 years	14	14	—
		$ 23,003	$ 8,908	$ 14,095

STEVEN MADDEN, LTD. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements – Unaudited
September 30, 2010
($ in thousands except share and per share data)

Note T – Goodwill and Intangible Assets (continued)

The estimated future amortization expense of purchased intangibles as of September 30, 2010 is as follows:

2010 (remaining three months)	$ 734
2011	2,412
2012	1,673
2013	1,673
2014	1,673
Thereafter	5,930
	$ 14,095

Note U – Comprehensive Income

Comprehensive income for the three- and nine-month periods ended September 30, 2010 includes unrealized gains on marketable securities of $1,090 and $1,746, and was $24,006 and $59,846, respectively. Comprehensive income for the comparable periods ended September 30, 2009 includes unrealized gains on marketable securities of $730 and $1,029, and was $18,561 and $37,581, respectively.

Note V – Commitments, Contingencies and Other

Legal proceedings:

(a) As previously disclosed, on June 24, 2009, The Center For Environmental Health filed a lawsuit, Center for Environmental Health v. Lulu NYC, LLC, Steve Madden, Ltd., Steve Madden Retail, Inc., et al., Case No. RG09459448, in California Superior Court, Alameda County, against the Company and dozens of other California retailers and vendors of leather, vinyl and/or imitation leather handbags, belts and shoes alleging that the retailers and vendors failed to warn that certain of such products may expose California citizens to lead and lead compounds. The parties have finalized the substance of a consent judgment, the terms of which are not material to the Company's Condensed Consolidated Financial Statements.

(b) As previously disclosed, on June 24, 2009, a class action lawsuit, Shahrzad Tahvilian, et al. v. Steve Madden Retail, Inc. and Steve Madden, Ltd., Case No. BC 414217, was filed in the Superior Court of California, Los Angeles County, against the Company and its wholly-owned subsidiary alleging violations of California labor laws including, among other things, failure to provide mandated meal breaks and overtime pay to employees as required. The parties have agreed to resolve the dispute in private mediation and, on August 31, 2010, entered into a memorandum of understanding which remains subject to court approval. The memorandum of understanding is not expected to be submitted to the court for approval until early 2011. Based on the proposed settlement, the Company has increased its reserve for this claim from $1,000 to $2,750.

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STEVEN MADDEN, LTD. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements – Unaudited
September 30, 2010
($ in thousands except share and per share data)

Note V – Commitments, Contingencies and Other (continued)

(c) As previously disclosed, on August 10, 2005, following the conclusion of an audit of the Company conducted by auditors for U.S. Customs and Border Protection ("U.S. Customs") during 2004 and 2005, U.S. Customs issued a report that asserts that certain commissions that the Company treated as "buying agents' commissions" (which are non-dutiable) should be treated as "selling agents' commissions" and hence are dutiable. Subsequently, U.S. Immigration and Customs Enforcement notified the Company's legal counsel that a formal investigation of the Company's importing practices had been commenced as a result of the audit. In September of 2007, U.S. Customs notified the Company that it had finalized its assessment of the underpaid duties at $1,400. The Company, with the advice of legal counsel, evaluated the liability in the case, including additional duties, interest and penalties, and believed that it was not likely to exceed $3,045, and accordingly, a reserve for this amount was recorded as of December 31, 2009. The Company contested the conclusions of the U.S. Customs audit and filed a request for review and issuance of rulings thereon by U.S. Customs Headquarters, Office of Regulations and Rulings, under internal advice procedures. On September 20, 2010, the Company was advised by legal counsel that U.S. Customs had issued a ruling in the matter, concluding that the commissions paid by the Company pursuant to buying agreements entered into by the Company and one of its two buying agents under review were bona fide buying-agent commissions and, therefore, were non-dutiable. With respect to the second buying agent, U.S. Customs also ruled that beginning in February of 2002, commissions paid by the Company were bona fide buying agent commissions and, therefore, were non-dutiable. However, U.S. Customs found that the Company's pre-2002 buying agreements with the second agent were legally insufficient to substantiate a buyer-buyer's agent relationship between the Company and the agent and that commissions paid to the second agent under such buying agreements, in fact, were dutiable. Currently, the Company is reviewing the ruling, its consequences and the Company's options with its legal counsel. On the basis of the U.S. Customs ruling, the Company has reevaluated the liability in the case and believes that it is not likely to exceed $1,248 and the reserve has been reduced from $3,045 to such amount as of September 30, 2010.

(d) The Company has been named as a defendant in certain other lawsuits in the normal course of business. In the opinion of management, after consulting with legal counsel, the liabilities, if any, resulting from these matters should not have a material effect on the Company's financial condition or results of operations. It is the policy of management to disclose the amount or range of reasonably possible losses in excess of recorded amounts.

Note W – Operating Segment Information

The Company operates the following business segments: Wholesale Footwear, Wholesale Accessories, Retail, First Cost and Licensing. The Wholesale Footwear segment, through sales to department stores, mid-tier retailers and specialty stores worldwide, derives revenue from sales of branded and private label women's, men's, girls' and children's footwear. The Wholesale Accessories segment, which includes branded and private label handbags, belts and small leather goods, derives revenue from sales to department, mid-tier and specialty stores worldwide. The Retail segment, through the operation of Company owned retail stores and the Company's website, derives revenue from sales of branded women's, men's and children's footwear, accessories and licensed products to consumers. The First Cost

segment represents activities of a subsidiary which earns commissions for serving as a buying agent and as a selling agent of footwear products to mass-market merchandisers, mid-tier department stores and other retailers with respect to their purchase of footwear. In the License segment, the Company licenses its Steve Madden® and Steven by Steve Madden® trademarks for use in connection with the manufacturing, marketing and sale of cold weather accessories, sunglasses, eyewear, outerwear, bedding, hosiery and women's fashion apparel and jewelry.

STEVEN MADDEN, LTD. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements – Unaudited
September 30, 2010
($ in thousands except share and per share data)

Note W – Operating Segment Information (continued)

As of and three months ended,	Wholesale Footwear	Wholesale Accessories	Total Wholesale	Retail	First Cost	Licensing	Consolidated
September 30, 2010:							
Net sales to external customers	$ 123,251	$ 29,801	$ 153,052	$ 31,066			$ 184,118
Gross profit	48,362	11,095	59,457	18,051			77,508
Commissions and licensing fees - net	—	—	—	—	$ 5,617	$ 970	6,587
Income (loss) from operations	27,503	5,043	32,546	(1,745)	5,617	970	37,388
Segment assets	$ 302,842	$ 72,078	374,920	42,964	12,130	—	430,014
Capital expenditures			$ 337	$ 711	$ —	$ —	$ 1,048
September 30, 2009:							
Net sales to external customers	$ 92,205	$ 19,752	$ 111,957	$ 28,181			$ 140,138
Gross profit	38,979	7,141	46,120	15,556			61,676
Commissions and licensing fees - net	—	—	—	—	$ 4,974	$ 752	5,726
Income (loss) from operations	20,100	3,129	23,229	(641)	4,974	752	28,314
Segment assets	$ 219,140	$ 42,139	261,279	46,452	8,559	—	316,290
Capital expenditures			$ 328	$ 410	$ —	$ —	$ 738

As of and nine months ended,	Wholesale Footwear	Wholesale Accessories	Total Wholesale	Retail	First Cost	Licensing	Consolidated
September 30, 2010:							
Net sales to external customers	$ 310,176	$ 75,161	$ 385,337	$ 89,053			$ 474,390
Gross profit	123,929	29,308	153,237	53,057			206,294
Commissions and licensing fees - net	—	—	—	—	$ 14,976	$ 3,024	18,000
Income (loss) from operations	65,045	12,169	77,214	(914)	14,976	3,024	94,300
Segment assets	$ 302,842	$ 72,078	374,920	42,964	12,130	—	430,014
			$ 814	$ 1,466	$ —	$ —	$ 2,280

Capital expenditures							
September 30, 2009:							
Net sales to external customers	$ 231,610	$ 49,829	$ 281,439	$ 82,600			$ 364,039
Gross profit	93,126	16,451	109,577	45,149			154,726
Commissions and licensing fees - net	—	—	—	—	$ 13,431	$ 2,562	15,993
Income (loss) from operations	41,765	5,929	47,694	(5,697)	13,431	2,562	57,990
Segment assets	$ 219,140	$ 42,139	261,279	46,452	8,559	—	316,290
Capital expenditures			$ 753	$ 1,650	$ —	$ —	$ 2,403

STEVEN MADDEN, LTD. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements – Unaudited
September 30, 2010
($ in thousands except share and per share data)

Note W – Operating Segment Information (continued)

Revenues by geographic area for the three- and nine-month periods ended September 30 are as follows:

	Three months ended September 30,		Nine months ended September 30,	
	2010	2009	2010	2009
Domestic	$ 172,334	$ 134,206	$ 448,993	$ 347,758
International	11,784	5,932	25,397	16,281
Total	$ 184,118	$ 140,138	$ 474,390	$ 364,039

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

The following discussion of the Company's financial condition and results of operations should be read in conjunction with the unaudited Financial Statements and Notes thereto appearing elsewhere in this Quarterly Report.

This Quarterly Report contains certain forward-looking statements as that term is defined in the federal securities laws. The events described in forward-looking statements contained in this Quarterly Report may not occur. Generally forward-looking statements relate to business plans or strategies, projected or anticipated benefits or other consequences of our plans or strategies, projected or anticipated benefits from acquisitions to be made by us, or projections involving anticipated revenues, earnings or other aspects of our operating results. The words "may", "will", "expect", "believe", "anticipate", "project", "plan", "intend", "estimate", and "continue", and their opposites and similar expres intended to identify forward-looking statements. We caution you that these statements are not guarantees of future performance or events and are subject to a number of uncertainties, risks and other influences, many of which are beyond our control, that may influence the accuracy of the statements and the projections upon which the statements are based. Factors that may affect our results include, but are not limited to, the risks and uncertainties discussed in our Annual Report on Form 10-K for the year ended December 31, 2009. Any one or more of these uncertainties, risks and other influences could materially affect our results of operations and whether forward-looking statements made by us ultimately prove to be accurate. Our actual results, performance and achievements could differ materially from those expressed or implied in these forward-looking statements. We undertake no obligation to publicly update or revise any forward-looking statements, whether from new information, future events or otherwise.

Overview:
($ in thousands, except retail sales data per square foot and earnings per share)

Steven Madden, Ltd. and its subsidiaries (the "Company") designs, sources, markets and retails fashion-forward footwear and accessories for women, men and children. We distribute products through department stores, specialty stores, luxury retailers, national chains, mass merchants, our retail stores and our e-commerce website throughout the United States as well as through special distribution arrangements in Canada, Europe, Central and South America, Australia and Asia. Our product line includes a broad range of updated styles which are designed to establish or capitalize on market trends, complemented by core products. We have established a reputation for our creative designs, popular styles and quality products at affordable price points.

On March 24, 2010, the Board of Directors declared a 3-for-2 stock split of the Company's outstanding shares of common stock, effected in the form of a stock dividend on the Company's outstanding common stock. Stockholders of record at the close of business on April 20, 2010 received one additional share of Steven Madden Ltd. common stock for every two shares of common stock owned on this date. The additional shares were distributed on May 3, 2010. Stockholders received cash in lieu of any fractional shares of common stock they otherwise would have received in connection with the dividend. All share and per share data provided herein gives effect to this stock split, applied retroactively.

On October 5, 2010, the Company acquired from Betsey Johnson LLC ("Betsey Johnson"), among other things, the Betsey Johnson® and Betseyville® trademarks through a series of transactions. First, on August 27, 2010, we

purchased from various members of a loan syndicate their respective participations in a term loan in the aggregate outstanding principal amount of $48,750 (the “Loan”) made by the syndicate lenders to Betsey Johnson. The Loan was originally made by the syndicate lenders to Betsey Johnson pursuant to a Loan and Security Agreement dated as of August 20, 2007 and provided for a maximum term loan amount of $50,000. The aggregate purchase price paid by the Company to the syndicate lenders for their participations in the Loan was $29,186 including transaction costs. The Loan, which was secured by a first priority security interest on substantially all assets of Betsey Johnson, was in default on the date of purchase. Then, on October 5, 2010, we entered into a Restructuring Agreement with Betsey Johnson. Pursuant to the Restructuring Agreement, in consideration of the elimination of all amounts owed under the Loan and Security Agreement, we acquired (i) the trademarks and other intellectual property of Betsey Johnson, including Betsey Johnson® and other related brand names, (ii) certain intellectual property licenses and (iii) a 10% equity interest in Betsey Johnson. Management believes that Betsey Johnson® is an iconic brand that offers meaningful growth opportunity for our business. Prior to its entry into the Restructuring Agreement, Betsey Johnson had licensed to the company the right to use the Betsey Johnson® and Betseyville® trademarks in connection with the sale and marketing of handbags, small leather goods and belts.

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Exercisable as of September 30, 2016

137,541

$

2.80

6.14

$

188,511

The weighted average grant date fair value per share of options granted during the nine months ended September 30, 2016 was $0.83. The total intrinsic value of stock options exercised during the nine months ended September 30, 2016 and 2015 was $59,531 and $85,387, respectively. During the nine months ended September 30, 2016, the number of net settled shares which were issued as a result of stock option exercises was 8,171.

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SIRIUS XM HOLDINGS INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
(UNAUDITED)
(Dollars and shares in thousands, except per share amounts)

We recognized share-based payment expense associated with stock options of $21,484 and $19,418 for the three months ended September 30, 2016 and 2015, respectively, and $59,510 and $52,662 for the nine months ended September 30, 2016 and 2015, respectively.

The following table summarizes the restricted stock unit, including performance-based restricted stock units ("PRSUs"), and stock award activity under our share-based plans for the nine months ended September 30, 2016:

	Shares	Grant Date Fair Value Per Share
Nonvested as of December 31, 2015	16,088	$ 3.73
Granted	17,453	$ 4.21
Vested	(4,009)	$ 3.66
Forfeited	(456)	$ 3.71
Nonvested as of September 30, 2016	29,076	$ 4.02

The total intrinsic value of restricted stock units and stock awards vesting during the nine months ended September 30, 2016 and 2015 was $16,890 and $9,565, respectively. During the nine months ended September 30, 2016, the number of net settled shares which were issued as a result of restricted stock units vesting and the number of shares issued from stock awards granted totaled 2,387.

On August 5, 2016, we granted 3,036 PRSUs to certain employees, the vesting of which is subject to the employee's continuing employment and our achievement of certain performance goals. The awards cliff vest on the three-year anniversary of the grant date. We believe it is probable that the performance target applicable to these PRSUs will be achieved.

We recognized share-based payment expense associated with restricted stock units and stock awards of $8,536 and $3,975 during the three months ended September 30, 2016 and 2015, respectively, and $18,380 and $9,672 for the nine months ended September 30, 2016 and 2015, respectively. The three months ended September 30, 2016 included $669 of compensation expense related to PRSUs.

Total unrecognized compensation costs related to unvested share-based payment awards for stock options and restricted stock units granted to employees, members of our board of directors and third parties at September 30, 2016 and December 31, 2015 were $281,678 and $261,628, respectively. The total unrecognized compensation costs at September 30, 2016 are expected to be recognized over a weighted-average period of 2.7 years.

401(k) Savings Plan

Sirius XM sponsors the Sirius XM Radio Inc. 401(k) Savings Plan (the “Sirius XM Plan”) for eligible employees. The Sirius XM Plan allows eligible employees to voluntarily contribute from 1% to 50% of their pre-tax eligible earnings, subject to certain defined limits. We match 50% of an employee’s voluntary contributions per pay period on the first 6% of an employee’s pre-tax salary up to a maximum of 3% of eligible compensation. We may also make additional discretionary matching, true-up matching and non-elective contributions to the Sirius XM Plan. Employer matching contributions under the Sirius XM Plan vest at a rate of 33.33% for each year of employment and are fully vested after three years of employment for all current and future contributions. Our cash employer matching contributions are not used to purchase shares of our common stock on the open market, unless the employee elects our common stock as their investment option for this contribution. We recognized $1,640 and $1,486 in expense during the three months ended September 30, 2016 and 2015, respectively, and $4,857 and $6,026 in expense during nine months ended September 30, 2016 and 2015, respectively.

Sirius XM Holdings Inc. Deferred Compensation Plan

In 2015, we adopted the Sirius XM Holdings Inc. Deferred Compensation Plan (the "DCP"). The DCP allows members of our board of directors and certain eligible employees to defer all or a portion of their base salary, cash incentive compensation and/or board of directors' compensation, as applicable, each plan year starting in 2016. Pursuant to the terms of the DCP, we may elect to make additional contributions beyond amounts deferred by participants, but we are under no obligation to do so. We have established a grantor (or "rabbi") trust to facilitate the payment of our obligations under the DCP.

SIRIUS XM HOLDINGS INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
(UNAUDITED)
(Dollars and shares in thousands, except per share amounts)

As of September 30, 2016, the fair value of the investments in the trust was $4,625, which is included in Other long-term assets in our unaudited consolidated balance sheets and is classified as trading securities. Trading gains and losses associated with the trust are recorded in Other income within our unaudited consolidated statements of comprehensive income. The associated liability is recorded within Other long-term liabilities in our unaudited consolidated balance sheets, and any increase or decrease in the liability is recorded in General and administration expense within our unaudited consolidated statements of comprehensive income.

(13) Commitments and Contingencies

The following table summarizes our expected contractual cash commitments as of September 30, 2016:

	2016	2017	2018	2019	2020	Thereafter	Total
Debt obligations	$359,733	$5,485	$4,477	$3,169	$791,328	$5,000,000	$6,164,192
Cash interest payments	69,363	348,034	340,140	340,041	328,098	1,058,688	2,484,364
Satellite and transmission	29,594	94,416	68,300	51,927	25,721	24,756	294,714
Programming and content	58,968	302,814	279,001	260,155	222,332	356,825	1,480,095
Marketing and distribution	9,163	17,304	15,744	12,986	7,445	7,400	70,042
Satellite incentive payments	3,176	13,296	14,302	10,652	9,310	79,785	130,521
Operating lease obligations	7,620	44,917	43,425	39,279	36,764	180,791	352,796
Other	21,175	25,515	8,519	1,209	380	40	56,838
Total [(1)]	$558,792	$851,781	$773,908	$719,418	$1,421,378	$6,708,285	$11,033,562

(1) The table does not include our reserve for uncertain tax positions, which at September 30, 2016 totaled $5,427, as the specific timing of any cash payments cannot be projected with reasonable certainty.

Debt obligations. Debt obligations include principal payments on outstanding debt and capital lease obligations.

Cash interest payments. Cash interest payments include interest due on outstanding debt and capital lease payments through maturity.

Satellite and transmission. We have entered into agreements with third parties to operate and maintain the off-site satellite telemetry, tracking and control facilities and certain components of our terrestrial repeater networks. During the quarter ended September 30, 2016, we entered into an agreement with Space Systems/Loral to design and build two replacement satellites, SXM-7 and SXM-8, for our service.

Programming and content. We have entered into various programming agreements. Under the terms of these agreements, our obligations include fixed payments, advertising commitments and revenue sharing arrangements. Our future revenue sharing costs are dependent upon many factors and are difficult to estimate; therefore, they are not included in our minimum contractual cash commitments.

Marketing and distribution. We have entered into various marketing, sponsorship and distribution agreements to promote our brand and are obligated to make payments to sponsors, retailers, automakers and radio manufacturers under these agreements. Certain programming and content agreements also require us to purchase advertising on properties owned or controlled by the licensors. We also reimburse automakers for certain engineering and development costs associated with the incorporation of satellite radios into new vehicles they manufacture.

Satellite incentive payments. Boeing Satellite Systems International, Inc., the manufacturer of certain of our in-orbit satellites, may be entitled to future in-orbit performance payments with respect to XM-3 and XM-4 meeting their fifteen-year design life, which we expect to occur. Boeing may also be entitled to additional incentive payments up to $10,000 if our XM-4 satellite continues to operate above baseline specifications during the five years beyond the satellite’s fifteen-year design life.

Space Systems/Loral, the manufacturer of certain of our in-orbit satellites, may be entitled to future in-orbit performance payments with respect to XM-5, FM-5 and FM-6 meeting their fifteen-year design life, which we expect

to occur.

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Operating lease obligations. We have entered into both cancelable and non-cancelable operating leases for office space, equipment and terrestrial repeaters. These leases provide for minimum lease payments, additional operating expense charges, leasehold improvements and rent escalations that have initial terms ranging from one to fifteen years, and certain leases have options to renew. The effect of the rent holidays and rent concessions are recognized on a straight-line basis over the lease term, including reasonably assured renewal periods.

Other. We have entered into various agreements with third parties for general operating purposes. In addition to the minimum contractual cash commitments described above, we have entered into agreements with other variable cost arrangements. These future costs are dependent upon many factors and are difficult to anticipate; however, these costs may be substantial. We may enter into additional programming, distribution, marketing and other agreements that contain similar variable cost provisions. The cost of our stock acquired but not paid for as of September 30, 2016 is also included in this category.

We do not have any other significant off-balance sheet financing arrangements that are reasonably likely to have a material effect on our financial condition, results of operations, liquidity, capital expenditures or capital resources.

Legal Proceedings

In the ordinary course of business, we are a defendant or party to various claims and lawsuits, including those discussed below.

We record a liability when we believe that it is both probable that a liability will be incurred, and the amount of loss can be reasonably estimated. We evaluate developments in legal matters that could affect the amount of liability that has been previously accrued and make adjustments as appropriate. Significant judgment is required to determine both probability and the estimated amount of a loss or potential loss. We may be unable to reasonably estimate the reasonably possible loss or range of loss for a particular legal contingency for various reasons, including, among others, because: (i) the damages sought are indeterminate; (ii) the proceedings are in the relative early stages; (iii) there is uncertainty as to the outcome of pending proceedings (including motions and appeals); (iv) there is uncertainty as to the likelihood of settlement and the outcome of any negotiations with respect thereto; (v) there remain significant factual issues to be determined or resolved; (vi) the relevant law is unsettled; or (vii) the proceedings involve novel or untested legal theories. In such instances, there may be considerable uncertainty regarding the ultimate resolution of such matters, including a possible eventual loss, if any.

Telephone Consumer Protection Act Suits. We are a defendant in several purported class action suits that allege that we, or call center vendors acting on our behalf, made calls which violate provisions of the Telephone Consumer Protection Act of 1991 (the “TCPA”). The plaintiffs in these actions allege, among other things, that we called mobile phones using an automatic telephone dialing system without the consumer’s prior consent or, alternatively, after the consumer revoked his or her prior consent. In one of the actions, the plaintiff also alleges that we violated the TCPA’s call time restrictions and, in one of the other actions, the plaintiff also alleges that we violated the TCPA’s do not call restrictions. These purported class action cases are titled Erik Knutson v. Sirius XM Radio Inc., No. 12-cv-0418-AJB-NLS (S.D. Cal.), Francis W. Hooker v. Sirius XM Radio Inc., No. 4:13-cv-3 (E.D. Va.), Yefim Elikman v. Sirius XM Radio Inc. and Career Horizons, Inc., No. 1:15-cv-02093 (N.D. Ill.), and Anthony Parker v. Sirius XM Radio Inc., No. 8:15-cv-01710-JSM-EAJ (M.D. Fla), and are described in Item 3., Legal Proceedings, in our Annual Report on Form 10-K for the year ended December 31, 2015.

We have entered into an agreement to settle these purported class action suits. The settlement is expected to resolve the claims of consumers beginning in February 2008 relating to telemarketing calls to their mobile telephones. As part of this settlement, we have made a $35,000 payment to a settlement fund (from which notice, administration and other costs and attorneys’ fees will be paid), and are offering participating class members the option of receiving three months of our Select service for no charge, and will enter into agreements to make modifications to the practices of certain call center vendors. The settlement is subject to final court approval, which cannot be assured.

Pre-1972 Sound Recording Matters. In August 2013, SoundExchange, Inc. filed a complaint in the United States District Court for the District of Columbia alleging that we underpaid royalties for statutory licenses during the 2007-2012 period in violation of the regulations established by the Copyright Royalty Board for that period. SoundExchange principally alleges that we improperly reduced our calculation of gross revenues, on which the royalty payments are based, by deducting non-recognized revenue attributable to pre-1972 recordings and Premier package revenue that is not "separately charged" as

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required by the regulations. SoundExchange is seeking compensatory damages of not less than $50,000 and up to $100,000 or more, payment of late fees and interest, and attorneys' fees and costs.
In August 2014, the United States District Court for the District of Columbia granted our motion to dismiss the complaint without prejudice on the grounds that the case properly should be pursued before the Copyright Royalty Board rather than the district court. In December 2014, SoundExchange filed a petition with the Copyright Royalty Board requesting an order interpreting the applicable regulations. We have submitted legal briefs and other evidence supporting our position that our payments and practices complied with the regulations established by the Copyright Royalty Board for statutory licenses during the 2007-2012 period or, in the event that the Judges should find that the applicable regulations were unclear, that the Judges should clarify the regulations and confirm that our payments and practices complied with the regulations for that period. Briefing in this matter is complete and a decision from the Copyright Royalty Board is pending.
This matter is titled SoundExchange, Inc. v. Sirius XM Radio, Inc., No.13-cv-1290-RJL (D.D.C.), and Determination of Rates and Terms for Preexisting Subscription Services and Satellite Digital Audio Radio Services, United States Copyright Royalty Board, No. 2006-1 CRB DSTRA. Information concerning the action is publicly available in filings under the docket numbers. The outcome of this matter is inherently unpredictable and subject to significant uncertainties, many of which are beyond our control. No provision was made for losses to the extent such are not probable and estimable. We believe we have substantial defenses to the claims asserted, and intend to defend this action vigorously.
Other Matters. In the ordinary course of business, we are a defendant in various other lawsuits and arbitration proceedings, including derivative actions; actions filed by subscribers, both on behalf of themselves and on a class action basis; former employees; parties to contracts or leases; and owners of patents, trademarks, copyrights or other intellectual property. None of these other matters, in our opinion, is likely to have a material adverse effect on our business, financial condition or results of operations.

(14) Income Taxes
We file a consolidated federal income tax return for all of our wholly-owned subsidiaries, including Sirius XM. For the three months ended September 30, 2016 and 2015, income tax expense was $111,556 and $112,543, respectively. For the nine months ended September 30, 2016 and 2015, income tax expense was $326,108 and $296,893, respectively.
Our effective tax rate for the three and nine months ended September 30, 2016 was 36.5% and 37.6%, respectively. Our effective tax rate for the three and nine months ended September 30, 2015 was 40.3% and 44.2%, respectively. Our effective tax rate for the nine months ended September 30, 2015 was impacted by tax law changes in the District of Columbia and New York City. The tax law change in the District of Columbia will reduce our future tax and thus we will use less of certain net operating losses in the future which resulted in a $44,392 increase in our valuation allowance during the three months ended March 31, 2015. The tax law change in New York City will increase certain net operating losses to be utilized in the future which resulted in a $14,831 increase in our deferred tax asset during the three months ended June 30, 2015.
As of September 30, 2016 and December 31, 2015, we had a valuation allowance related to deferred tax assets of $49,257 and $49,095, respectively, that were not likely to be realized due to certain net operating loss limitations and acquired net operating losses that were not more likely than not going to be utilized.

(15) Subsequent Events
Debt Redemption

On October 1, 2016, we redeemed $650,000 in principal amount of our outstanding 5.875% Notes for an approximate purchase price of $669,097, including premium, which will result in the recognition of a Loss on extinguishment of debt and credit facilities, net, of approximately $24,229 in the fourth quarter of 2016. This redemption was funded with $359,097 of Cash and cash equivalents and $310,000 of additional borrowings under our Credit Facility.

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Capital Return Program

For the period from October 1, 2016 to October 25, 2016, we repurchased 18,548 shares of our common stock on the open market for an aggregate purchase price of $76,791, including fees and commissions.

On October 26, 2016, our board of directors approved an additional $2,000,000 for repurchase of our common stock. The new approval increases the amount of common stock that we have been authorized to repurchase to an aggregate of $10,000,000. Shares of common stock may be purchased from time to time on the open market and in privately negotiated transactions, including in accelerated stock repurchase transactions and transactions with Liberty Media and its affiliates. We intend to fund the additional repurchases through a combination of cash on hand, cash generated by operations and future borrowings.

On October 26, 2016, our board of directors also declared the first quarterly dividend on our common stock in the amount of $0.01 per share of common stock payable on November 30, 2016 to stockholders of record as of the close of business on November 9, 2016. Our board of directors expects that this dividend will be the first of regular quarterly dividends, in an aggregate annual amount of $0.04 per share of common stock.

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

All amounts referenced in this Item 2 are in thousands, except per subscriber and per installation amounts, unless otherwise stated.

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our unaudited consolidated financial statements and related notes included elsewhere in this Quarterly Report on Form 10-Q and with our Annual Report on Form 10-K for the year ended December 31, 2015.

Special Note Regarding Forward-Looking Statements

The following cautionary statements identify important factors that could cause our actual results to differ materially from those projected in forward-looking statements made in this Quarterly Report on Form 10-Q and in other reports and documents published by us from time to time. Any statements about our beliefs, plans, objectives, expectations, assumptions, future events or performance are not historical facts and may be forward-looking. These statements are often, but not always, made through the use of words or phrases such as "will likely result," "are expected to," "will continue," "is anticipated," "estimated," "intend," "plan," "projection" and "outlook." Any forward-looking statements are qua in their entirety by reference to the factors discussed throughout this Quarterly Report on Form 10-Q and in other reports and documents published by us from time to time, particularly the risk factors described under "Risk Factors" in Part I, Item 1A, of our Annual Report on Form 10-K for the year ended December 31, 2015 and "Management's Discussion and Analysis of Financial Condition and Results or Operations" herein and in Part II, Item 7, of our Annual Report on Form 10-K for the year ended December 31, 2015.

Among the significant factors that could cause our actual results to differ materially from those expressed in the forward-looking statements are:

- we face substantial competition and that competition is likely to increase over time;
- our ability to attract and retain subscribers in the future is uncertain;
- consumer protection laws and their enforcement could damage our business;
- the unfavorable outcome of pending or future litigation;
- the market for music rights is changing and is subject to significant uncertainties;
- our business depends in large part upon the auto industry;
- general economic conditions can affect our business;
- if we fail to protect the security of personal information about our customers, we could be subject to costly government enforcement actions and private litigation and our reputation could suffer;
- other existing or future government laws and regulations could harm our business;
- failure of our satellites would significantly damage our business;
- interruption or failure of our information technology and communications systems could negatively impact our results and our brand;
- we may not realize the benefits of acquisitions or other strategic initiatives;
- rapid technological and industry changes could adversely impact our services;
- failure of third parties to perform could adversely affect our business;
- our service may experience harmful interference from new and existing wireless operations;
- failure to comply with FCC requirements could damage our business;
- we may from time to time modify our business plan, and these changes could adversely affect us and our financial condition;
- we have a significant amount of indebtedness, and our revolving credit facility contains certain covenants that restrict our current and future operations;

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- our studios, terrestrial repeater networks, satellite uplink facilities or other ground facilities could be damaged by natural catastrophes or terrorist activities;
- our principal stockholder has significant influence, including over actions requiring stockholder approval, and its interests may differ from the interests of other holders of our common stock;
- we are a “controlled company” within the meaning of the NASDAQ listing rules and, as a result, qualify for, and rely on, exemptions from certain corporate governance requirements; and
- our business may be impaired by third-party intellectual property rights.

Because the risk factors referred to above could cause actual results or outcomes to differ materially from those expressed in any forward-looking statements made by us or on our behalf, you should not place undue reliance on any of these forward-looking statements. In addition, any forward-looking statement speaks only as of the date on which it is made, and we undertake no obligation to update any forward-looking statement or statements to reflect events or circumstances after the date on which the statement is made, to reflect the occurrence of unanticipated events or otherwise, except as required by law. New factors emerge from time to time, and it is not possible for us to predict which will arise or to assess with any precision the impact of each factor on our business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements.

Executive Summary

We transmit music, sports, entertainment, comedy, talk, news, traffic and weather channels, as well as infotainment services, in the United States on a subscription fee basis through our two proprietary satellite radio systems. Subscribers can also receive music and other channels, plus features such as SiriusXM On Demand and MySXM, over our Internet radio service, including through applications for mobile devices. We are also a leader in providing connected vehicle services. Our connected vehicle services are designed to enhance the safety, security and driving experience for vehicle operators while providing marketing and operational benefits to automakers and their dealers.

We have agreements with every major automaker (“OEMs”) to offer satellite radio in their vehicles. We also acquire subscribers through marketing to owners and lessees of previously owned vehicles that include factory-installed satellite radios that are not currently subscribing to our services. Additionally, we distribute our satellite radios through retailers online and at locations nationwide and through our website. Satellite radio services are also offered to customers of certain rental car companies.

As of September 30, 2016, we had approximately 31.0 million subscribers of which approximately 25.5 million were self-pay subscribers and approximately 5.5 million were paid promotional subscribers. Our subscriber totals include subscribers under our regular pricing plans; discounted pricing plans; subscribers that have prepaid, including payments either made or due from automakers for subscriptions included in the sale or lease price of a vehicle; subscribers to our Internet services who do not also have satellite radio subscriptions; and certain subscribers to our weather, traffic, and data services who do not also have satellite radio subscriptions. Subscribers and subscription related revenues and expenses associated with our connected vehicle services and the Sirius XM Canada service are not included in our subscriber count or subscriber-based operating metrics.

Our primary source of revenue is subscription fees, with most of our customers subscribing on an annual, semi-annual, quarterly or monthly plan. We offer discounts for prepaid, longer term subscription plans, as well as a multiple subscription discount. We also derive revenue from activation and other fees, the sale of advertising on select non-music channels, the direct sale of satellite radios and accessories, and other ancillary services, such as our weather, traffic and data services.

In certain cases, a subscription to our radio services is included in the sale or lease price of new vehicles or previously owned vehicles. The length of these subscriptions varies but is typically three to twelve months. We receive payments for these subscriptions from certain automakers. We also reimburse various automakers for certain costs associated with satellite radios installed in new vehicles.

As of September 30, 2016, Liberty Media beneficially owned, directly and indirectly, approximately 65% of the outstanding shares of our common stock. As a result, we are a “controlled company” for the purposes of the NASDAQ corporate governance requirements. Liberty Media owns interests in a range of media, communications and entertainment businesses.

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Recent Development

Recapitalization of Sirius XM Canada

On May 12, 2016, our subsidiary, Sirius XM Radio Inc. (“Sirius XM”), entered into an arrangement agreement (the “Arrangement Agreement”) with Sirius XM Canada Holdings Inc. ("Sirius XM Canada"), an entity in which Sirius XM currently holds an approximate 37% economic interest and 25% voting interest. Pursuant to the Arrangement Agreement, Sirius XM and certain Canadian shareholders will form a new company to acquire shares of Sirius XM Canada not already owned by them pursuant to a plan of arrangement (the “Transaction”). In connection with the Transaction, Sirius XM Canada’s shareholders will be entitled to elect to receive, for each share of Sirius XM Canada held, C$4.50 (U.S. $3.50 as of May 12, 2016) in (i) cash, (ii) shares of our common stock, (iii) a security exchangeable for shares of our common stock, or (iv) a combination thereof; provided that no more than 50% of the total consideration in the Transaction (or up to 35,000 shares) will be issued in our common stock and exchangeable shares. All of the obligations of Sirius XM under the Arrangement Agreement are guaranteed by us.

Following the Transaction, Sirius XM is expected to hold a 70% economic interest and 33% voting interest in Sirius XM Canada, with the remainder of the voting power and economic interest held by Slaight Communications and Obelysk Media, two of Sirius XM Canada’s current Canadian shareholders. Sirius XM expects to contribute to Sirius XM Canada approximately U.S. $275,000 in connection with the Transaction (assuming that all shareholders elect to receive cash in connection with the Transaction), which amount is expected to be used to pay the cash consideration to Sirius XM Canada’s shareholders and will be decreased proportionately if shareholders elect to receive consideration in shares of our common stock or securities exchangeable for our common stock.

The Transaction has been approved by the stockholders of Sirius XM Canada and has received the required court approval. The Transaction remains subject to receipt of Canadian Radio-Television and Telecommunications Commission approval. Pending receipt of this approval, the Transaction is expected to close in the fourth quarter of 2016.

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Results of Operations

Set forth below are our results of operations for the three and nine months ended September 30, 2016 compared with the three and nine months ended September 30, 2015.

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,		2016 vs 2015 Change			
					Three Months		Nine Months	
	2016	2015	2016	2015	Amount	%	Amount	%
Revenue:								
Subscriber revenue	$1,069,746	$974,471	$3,112,712	$2,826,018	$95,275	10 %	$286,694	10 %
Advertising revenue	34,268	33,131	99,330	88,843	1,137	3 %	10,487	12 %
Equipment revenue	31,306	25,875	86,285	79,979	5,431	21 %	6,306	8 %
Other revenue	142,326	136,235	415,895	379,072	6,091	4 %	36,823	10 %
Total revenue	1,277,646	1,169,712	3,714,222	3,373,912	107,934	9 %	340,310	10 %
Operating expenses:								
Cost of services:								
Revenue share and royalties	272,823	238,620	788,952	783,115	34,203	14 %	5,837	1 %
Programming and content	89,015	75,707	257,760	216,223	13,308	18 %	41,537	19 %
Customer service and billing	94,923	94,492	285,502	278,521	431	0 %	6,981	3 %
Satellite and transmission	22,224	22,743	80,609	65,761	(519)	(2)%	14,848	23 %
Cost of equipment	9,674	9,246	29,181	29,021	428	5 %	160	1 %
Subscriber acquisition costs	120,111	133,009	381,516	391,773	(12,898)	(10)%	(10,257)	(3)%
Sales and marketing	99,194	90,541	279,278	255,778	8,653	10 %	23,500	9 %
Engineering, design and development	19,254	16,132	57,588	47,180	3,122	19 %	10,408	22 %
General and administrative	90,369	67,234	249,052	219,194	23,135	34 %	29,858	14 %
Depreciation and amortization	67,880	70,404	202,215	202,527	(2,524)	(4)%	(312)	0 %
Total operating expenses	885,467	818,128	2,611,653	2,489,093	67,339	8 %	122,560	5 %
Income from operations	392,179	351,584	1,102,569	884,819	40,595	12 %	217,750	25 %
Other income (expense):								
Interest expense	(89,092)	(76,624)	(250,888)	(221,912)	(12,468)	(16)%	(28,976)	(13)%
Other income	2,370	4,133	15,733	9,077	(1,763)	(43)%	6,656	73 %
Total other expense	(86,722)	(72,491)	(235,155)	(212,835)	(14,231)	(20)%	(22,320)	(10)%
Income before income taxes	305,457	279,093	867,414	671,984	26,364	9 %	195,430	29 %
Income tax expense	(111,556)	(112,543)	(326,108)	(296,893)	987	1 %	(29,215)	(10)%
Net income	$193,901	$166,550	$541,306	$375,091	$27,351	16 %	$166,215	44 %

Total Revenue

Subscriber Revenue includes subscription, activation and other fees.

For the three months ended September 30, 2016 and 2015, subscriber revenue was $1,069,746 and $974,471, respectively, an increase of 10%, or $95,275. For the nine months ended September 30, 2016 and 2015, subscriber revenue was $3,112,712 and $2,826,018, respectively, an increase of 10%, or $286,694. The period over period increase was primarily attributable to a 7% and 8% increase in daily weighted average number of subscribers for the three and

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nine months ended September 30, 2016, respectively, as well as a 3% increase in average monthly revenue per subscriber resulting from our price changes and mix of plans.
We expect subscriber revenues to increase based on the growth of our subscriber base, the effects of increases in certain of our subscription rates and the sale of additional services to subscribers.
Advertising Revenue includes the sale of advertising on certain non-music channels.
For the three months ended September 30, 2016 and 2015, advertising revenue was $34,268 and $33,131, respectively, an increase of 3%, or $1,137. For the nine months ended September 30, 2016 and 2015, advertising revenue was $99,330 and $88,843, respectively, an increase of 12%, or $10,487. For the three months ended September 30, 2016, the increase was primarily due to a greater number of advertising spots sold and transmitted, partially offset by the loss of a significant advertiser due to state regulatory activities surrounding the fantasy sports industry. For the nine months ended September 30, 2016, the increase was primarily due to a greater number of advertising spots sold and transmitted as well as increased rates per spot.
We expect our advertising revenue to continue to grow as more advertisers are attracted to our national platform and growing subscriber base and as we launch additional non-music channels.
Equipment Revenue includes revenue and royalties from the sale of satellite radios, components and accessories.
For the three months ended September 30, 2016 and 2015, equipment revenue was $31,306 and $25,875, respectively, an increase of 21%, or $5,431. For the nine months ended September 30, 2016 and 2015, equipment revenue was $86,285 and $79,979, respectively, an increase of 8%, or $6,306. The period over period increase for the three months and nine months ended September 30, 2016 was driven by an increase in OEM production and an increase in royalty revenue on certain modules starting early in the second quarter of 2016, partially offset by lower sales through our aftermarket and direct to consumer businesses.
We expect equipment revenue to fluctuate based on OEM production for which we receive royalty payments for our technology and, to a lesser extent, on the volume of equipment sales in our aftermarket and direct to consumer businesses.
Other Revenue includes amounts earned from subscribers for the U.S. Music Royalty Fee, and revenue from our connected vehicle services, our Canadian affiliate and ancillary revenues.
For the three months ended September 30, 2016 and 2015, other revenue was $142,326 and $136,235, respectively, an increase of 4%, or $6,091. For the nine months ended September 30, 2016 and 2015, other revenue was $415,895 and $379,072, respectively, an increase of 10%, or $36,823. The period over period increase was primarily driven by revenues from the U.S. Music Royalty Fee due to an increase in the number of subscribers and subscribers paying at a higher rate. These increases were offset by lower activation revenues and a change in a programming contract in the third quarter of 2015 related to our Canadian affiliate and the timing of non-recurring engineering fees from our connected vehicle services.
We expect other revenue to increase as our growing subscriber base drives higher U.S. Music Royalty Fees.
Operating Expenses
Revenue Share and Royalties include distribution and content provider revenue share, royalties for transmitting content and web streaming, and advertising revenue share.
For the three months ended September 30, 2016 and 2015, revenue share and royalties were $272,823 and $238,620, respectively, an increase of 14%, or $34,203, and increased as a percentage of total revenue. For the nine months ended September 30, 2016 and 2015, revenue share and royalties were $788,952 and $783,115, respectively, an increase of 1%, or $5,837, but decreased as a percentage of total revenue. The increase for the three and nine month period was due to overall greater revenues subject to royalty and revenue sharing arrangements, and a 5% increase in the statutory royalty rate applicable to our use of post-1972 recordings. The increase in the nine month period was mitigated by the impact of $116,639 in expense recorded during the nine months ended September 30, 2015 for the portion of the $210,000 settlement of the Capitol Records LLC et al. v. Sirius XM Radio Inc. lawsuit related to our use of pre-1972 sound recordings through September 30, 2015. We have recorded approximately $29,654 related to this settlement through the nine months ended September 30, 2016.

We expect our revenue share and royalty costs to increase as our revenues grow and as the statutory royalty rate applicable to post-1972 sound recordings increases. For the remainder of 2016 and in 2017, we expect to recognize $10,154 and $43,442, respectively, in expense related to the settlement relating to the use of pre-1972 sound recordings. As determined by the Copyright Royalty Board, we have paid or will pay royalties for the use of certain post-1972 sound recordings on our satellite radio service of 10.0%, 10.5% and 11% in 2015, 2016 and 2017, respectively.

Programming and Content includes costs to acquire, create, promote and produce content. We have entered into various agreements with third parties for music and non-music programming that require us to pay license fees and other amounts.

For the three months ended September 30, 2016 and 2015, programming and content expenses were $89,015 and $75,707, respectively, an increase of 18%, or $13,308, and increased as a percentage of total revenue. For the nine months ended September 30, 2016 and 2015, programming and content expenses were $257,760 and $216,223, respectively, an increase of 19%, or $41,537, and increased as a percentage of total revenue. The period over period increases were primarily due to renewed programming licenses as well as increased personnel related costs.

We expect our programming and content expenses to increase as we offer additional programming, and renew or replace expiring agreements.

Customer Service and Billing includes costs associated with the operation and management of internal and third party customer service centers, and our subscriber management systems as well as billing and collection costs, bad debt expense, and transaction fees.

For the three months ended September 30, 2016 and 2015, customer service and billing expenses were $94,923 and $94,492, respectively, an increase of less than 1%, or $431, but decreased as a percentage of total revenue. For the nine months ended September 30, 2016 and 2015, customer services and billing expenses were $285,502 and $278,521, respectively, an increase of 3%, or $6,981, but decreased as a percentage of total revenue. The period over period increases were primarily due to costs associated with a higher subscriber base driving greater bad debt expenses, transaction fees, and call center costs, partially offset by lower personnel related costs and classifying wireless transmission costs related to our connected vehicle services to Satellite and transmission expense in 2016.

We expect our customer service and billing expenses to increase as our subscriber base grows.

Satellite and Transmission consists of costs associated with the operation and maintenance of our terrestrial repeater networks; satellites; satellite telemetry, tracking and control systems; satellite uplink facilities; studios; and delivery of our Internet streaming and connected vehicle services.

For the three months ended September 30, 2016 and 2015, satellite and transmission expenses were $22,224 and $22,743, respectively, a decrease of 2%, or $519, and decreased as a percentage of total revenue. For the nine months ended September 30, 2016 and 2015, satellite and transmission expenses were $80,609 and $65,761, respectively, an increase of 23%, or $14,848, and increased as a percentage of revenue. The decrease in the three month period was driven primarily by lower web streaming costs from insourcing certain activities and repeater costs, offset by the inclusion of wireless transmission costs related to our connected vehicle services that were previously recorded to Customer service and billing expense in 2015. The increase for the nine month period was primarily due to the loss on disposal of certain obsolete satellite parts of $12,912, recorded in the three months ended June 30, 2016.

We expect satellite and transmission expenses, net of losses on disposals of assets, to remain relatively flat.

Cost of Equipment includes costs from the sale of satellite radios, components and accessories and provisions for inventory allowance attributable to products purchased for resale in our direct to consumer distribution channels.

For the three months ended September 30, 2016 and 2015, cost of equipment was $9,674 and $9,246, respectively, an increase of 5%, or $428, but decreased as a percentage of equipment revenue. For the nine months ended September 30, 2016 and 2015, cost of equipment was $29,181 and $29,021, respectively, an increase of 1%, or $160, but decreased as a percentage of equipment revenue.

We expect cost of equipment to fluctuate with changes in sales and inventory valuations.

Subscriber Acquisition Costs include hardware subsidies paid to radio manufacturers, distributors and automakers; subsidies paid for chipsets and certain other components used in manufacturing radios; device royalties for certain radios and

chipsets; commissions paid to automakers and retailers; product warranty obligations; freight; and provisions for inventory allowances attributable to inventory consumed in our OEM and retail distribution channels. The majority of subscriber acquisition costs are incurred and expensed in advance of, or concurrent with, acquiring a subscriber. Subscriber acquisition costs do not include advertising costs, marketing, loyalty payments to distributors and dealers of satellite radios or revenue share payments to automakers and retailers of satellite radios.

For the three months ended September 30, 2016 and 2015, subscriber acquisition costs were $120,111 and $133,009, respectively, a decrease of 10%, or $12,898, and decreased as a percentage of total revenue. For the nine months ended September 30, 2016 and 2015, subscriber acquisition costs were $381,516 and $391,773, respectively, a decrease of 3%, or $10,257, and decreased as a percentage of total revenue. The period over period decrease for the three months ended September 30, 2016 was driven by lower OEM hardware subsidies, a contractual reduction to a subsidy rate, and lower subsidized costs related to the transition of chipsets, partially offset by higher radio installations. The period over period decrease for the nine months ended September 30, 2016 was driven by a contractual reduction to a subsidy rate, and lower subsidized costs related to the transition of chipsets, partially offset by higher radio installations and related OEM hardware subsidies.

We expect subscriber acquisition costs to fluctuate with OEM installations and aftermarket volume; however, the cost of subsidized radio components is expected to decline. We intend to continue to offer subsidies, commissions and other incentives to acquire subscribers.

Sales and Marketing includes costs for marketing, advertising, media and production, including promotional events and sponsorships; cooperative marketing; and personnel. Marketing costs include expenses related to direct mail, outbound telemarketing and email communications.

For the three months ended September 30, 2016 and 2015, sales and marketing expenses were $99,194 and $90,541, respectively, an increase of 10%, or $8,653, and increased as a percentage of total revenue. For the nine months ended September 30, 2016 and 2015, sales and marketing expenses were $279,278 and $255,778, respectively, an increase of 9%, or $23,500, but decreased as a percentage of total revenue. The period over period increases for the three and nine months ended September 30, 2016 were primarily due to increased subscriber retention and acquisition campaigns related to our subscriber growth as well as higher personnel costs.

We anticipate that sales and marketing expenses will increase as we expand programs to retain our existing subscribers, win back former subscribers and attract new subscribers.

Engineering, Design and Development consists primarily of compensation and related costs to develop chipsets and new products and services, including streaming and connected vehicle services, research and development for broadcast information systems and costs associated with the incorporation of our radios into new vehicles manufactured by automakers.

For the three months ended September 30, 2016 and 2015, engineering, design and development expenses were $19,254 and $16,132, respectively, an increase of 19%, or $3,122, and increased as a percentage of total revenue. For the nine months ended September 30, 2016 and 2015, engineering, design and development expenses were $57,588 and $47,180, respectively, an increase of 22%, or $10,408, and increased as a percentage of total revenue. The period over period increases for the three and nine months ended September 30, 2016 were driven primarily by the inclusion of personnel related costs from our connected vehicle services that were previously recorded in Sales and marketing and General and administrative expense in 2015, partially offset by lower research and development costs.

We expect engineering, design and development expenses to increase in future periods as we continue to develop our infrastructure, products and services.

General and Administrative primarily consists of compensation and related costs for personnel and facilities, and include costs related to our finance, legal, human resources and information technologies departments.

For the three months ended September 30, 2016 and 2015, general and administrative expenses were $90,369 and $67,234, respectively, an increase of 34%, or $23,135, and increased as a percentage of total revenue. For the nine months ended September 30, 2016 and 2015, general and administrative expenses were $249,052 and $219,194, respectively, an increase of 14%, or $29,858, and increased as a percentage of total revenue. The period over period increases for the three and nine months ended September 30, 2016 were primarily driven by higher consulting and legal costs. Costs in the three months ended September 30, 2015, benefited from insurance recoveries related to a legal

settlement.

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We expect our general and administrative expenses to increase in future periods as a result of, among other things, enhanced information technology, on-going legal costs and personnel costs to support the growth of our business.
Depreciation and Amortization represents the recognition in earnings of the cost of assets used in operations, including our satellite constellations, property, equipment and intangible assets, over their estimated service lives.
For the three months ended September 30, 2016 and 2015, depreciation and amortization expense was $67,880 and $70,404, respectively, a decrease of 4%, or $2,524, and decreased as a percentage of total revenue. For the nine months ended September 30, 2016 and 2015, depreciation and amortization expense was $202,215 and $202,527, respectively, a decrease of less than 1%, or $312, and decreased as a percentage of total revenue. The decrease for the three month period was driven by certain satellites and software reaching the end of their estimated lives in 2015, partially offset by additional software and terrestrial repeater assets placed in service.
Other Income (Expense)
Interest Expense includes interest on outstanding debt.
For the three months ended September 30, 2016 and 2015, interest expense was $89,092 and $76,624, respectively, an increase of 16%, or $12,468. For the nine months ended September 30, 2016 and 2015, interest expense was $250,888 and $221,912, respectively, an increase of 13%, or $28,976. The increase was primarily due to higher average debt during the three and nine months ended September 30, 2016 compared to the three and nine months ended September 30, 2015.
We expect interest expense to increase in future periods to the extent our total debt outstanding increases.
Other Income primarily includes realized gains and losses, interest income, and our share of the income or loss of Sirius XM Canada.
For the three months ended September 30, 2016 and 2015, interest and investment income was $2,370 and $4,133, respectively. For the nine months ended September 30, 2016 and 2015, interest and investment income was $15,733 and $9,077, respectively. The income for the three and nine months ended September 30, 2016 was driven by our share of Sirius XM Canada’s net income. The nine months ended September 30, 2016 also included dividends received from Sirius XM Canada in excess of our investment. Pursuant to the Arrangement Agreement, Sirius XM Canada did not pay any dividends during the three months ended September 30, 2016. The income for the three and nine months ended September 30, 2015 was driven by the dividends received from Sirius XM Canada in excess of our investment.
Income Taxes
Income Tax Expense includes the change in our deferred tax assets, foreign withholding taxes and current federal and state tax expenses.
For the three months ended September 30, 2016 and 2015, income tax expense was $111,556 and $112,543, respectively. For the nine months ended September 30, 2016 and 2015, income tax expense was $326,108 and $296,893, respectively.
Our effective tax rate for the three and nine months ended September 30, 2016 was 36.5% and 37.6%, respectively. We estimate our annual effective tax rate for the year ending December 31, 2016 will be approximately 32% as we expect to recognize a Federal R&D tax credit in the fourth quarter of 2016 relating to the Protecting Americans from Tax Hikes Act of 2015. Our effective tax rate for the three and nine months ended September 30, 2015 was 40.3% and 44.2%, respectively. Our effective tax rate for the nine months ended September 30, 2015 was impacted by tax law changes in the District of Columbia and New York City. The tax law change in the District of Columbia will reduce our future tax and thus we will use less of certain net operating losses in the future which resulted in a $44,392 increase in our valuation allowance during the three months ended March 31, 2015. The tax law change in New York City will increase certain net operating losses to be utilized in the future which resulted in a $14,831 increase in our deferred tax asset during the three months ended June 30, 2015.
Key Financial and Operating Performance Metrics
In this section, we present certain financial performance measures that are not calculated and presented in accordance with generally accepted accounting principles in the United States (“Non-GAAP”), which include free cash flow and adjusted

EBITDA. We also present certain operating performance measures, which include average monthly revenue per subscriber, or ARPU; customer service and billing expenses, per average subscriber; and subscriber acquisition cost, or SAC, per installation. To the extent applicable, these measures exclude the impact of share-based payment expense and certain purchase price accounting adjustments related to the merger of Sirius and XM (the "Merger"). Additionally, when applicable, our adjusted EBITDA and free cash flow metrics exclude the effect of significant items that do not relate to the on-going performance of our business. We use these Non-GAAP financial and operating performance measures to manage our business, to set operational goals and as a basis for determining performance-based compensation for our employees. See accompanying glossary on pages 39 through 41 for more details and for the reconciliation to the most directly comparable GAAP measure (where applicable).

We believe these Non-GAAP financial and operating performance measures provide useful information to investors regarding our financial condition and results of operations. We believe investors find these Non-GAAP financial and operating performance measures useful in evaluating our core trends because they provide a direct view of our underlying contractual costs. We believe investors use our adjusted EBITDA to estimate our current enterprise value and to make investment decisions. We believe free cash flow provides useful supplemental information to investors regarding our cash available for future subscriber acquisition and capital expenditures, to repurchase or retire debt, to acquire other companies and to evaluate our ability to return capital to stockholders. By providing these Non-GAAP financial and operating performance measures, together with the reconciliations to the most directly comparable GAAP measure (where applicable), we believe we are enhancing investors' understanding of our business and our results of operations.

Our Non-GAAP financial measures should be viewed in addition to, and not as an alternative for or superior to, our reported results prepared in accordance with GAAP. In addition, our Non-GAAP financial measures may not be comparable to similarly-titled measures by other companies. Please refer to the glossary (pages 39 through 41) for a further discussion of such Non-GAAP financial and operating performance measures and reconciliations to the most directly comparable GAAP measure (where applicable). Subscribers and subscription related revenues and expenses associated with our connected vehicle services are not included in our subscriber count or subscriber-based operating metrics.

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Set forth below are our subscriber balances as of September 30, 2016 compared to September 30, 2015:

	As of September 30,		2016 vs 2015 Change	
	2016	2015	Amount	%
Self-pay subscribers	25,528	23,816	1,712	7%
Paid promotional subscribers	5,463	5,143	320	6%
Ending subscribers [(a)]	30,991	28,960	2,031	7%

(a) Amounts may not sum as a result of rounding.

The following table contains our Non-GAAP financial and operating performance measures which are based on our adjusted results of operations for the three and nine months ended September 30, 2016 and 2015:

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,		2016 vs 2015 Change			
					Three Months		Nine Months	
	2016	2015	2016	2015	Amount	%	Amount	%
Self-pay subscribers	385	381	1,240	1,293	4	1 %	(53)	(4)%
Paid promotional subscribers	(39)	145	157	355	(184)	(127)%	(198)	(56)%
Net additions [(a)]	345	525	1,397	1,649	(180)	(34)%	(252)	(15)%
Daily weighted average number of subscribers	30,776	28,649	30,290	28,033	2,127	7 %	2,257	8 %
Average self-pay monthly churn	1.9 %	1.9 %	1.8 %	1.8 %	0 %	0 %	0 %	0 %
New vehicle consumer conversion rate	40 %	41 %	39 %	41 %	(1)%	(2)%	(2)%	(5)%
ARPU	$13.04	$12.67	$12.83	$12.45	$0.37	3 %	$0.38	3 %
SAC, per installation	$28	$34	$31	$33	$(6)	(18)%	$(2)	(6)%
Customer service and billing expenses, per average subscriber	$0.97	$1.00	$0.98	$1.00	$(0.03)	(3)%	$(0.02)	(2)%
Adjusted EBITDA	$491,892	$447,194	$1,401,024	$1,261,382	$44,698	10 %	$139,642	11 %
Free cash flow	$356,527	$368,899	$1,079,690	$1,016,045	$(12,372)	(3)%	$63,645	6 %
Diluted weighted average common shares outstanding (GAAP)	4,919,829	5,346,438	5,005,133	5,487,116	(426,609)	(8)%	(481,983)	(9)%

(a) Amounts may not sum as a result of rounding.

Subscribers. At September 30, 2016, we had approximately 31.0 million subscribers, an increase of 2.0 million subscribers, or 7%, from the approximately 29.0 million subscribers as of September 30, 2015. The increase in total subscribers was primarily due to growth in our self-pay subscriber base, which increased 1.7 million. The increase in self-pay subscribers is primarily from original and subsequent owner trial conversions and subscriber win back programs, partially offset by deactivations. Our increase in paid promotional subscribers of 320 thousand subscribers resulted from the shipment of additional vehicles by OEMs offering paid trials.

For the three months ended September 30, 2016 and 2015, net additions were 345 thousand and 525 thousand, respectively, a decrease of 34%. For the nine months ended September 30, 2016 and 2015, net additions were 1,397 thousand and 1,649 thousand, respectively, a decrease of 15%. The period over period decrease for the three and nine months ended September 30, 2016 was due to a decrease in net additions of paid promotional subscribers as a result of slower growth in vehicle sales. Self-pay net additions increased slightly during the three months ended September 30, 2016 and decreased 4% for the nine months ended September 30, 2016. For the nine months ended September 30, 2016, the decrease in self-pay net additions was due to increases in deactivations from our larger subscriber base which were largely offset by increases in trial conversions and subscriber win back programs.

Average Self-pay Monthly Churn is derived by dividing the monthly average of self-pay deactivations for the period by the average number of self-pay subscribers for the period. (See accompanying glossary on pages 39 through 41 for more details.)

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For the three months ended September 30, 2016 and 2015, our average self-pay monthly churn rate was 1.9%. For the nine months ended September 30, 2016 and 2015, our average self-pay monthly churn rate was 1.8%.
New Vehicle Consumer Conversion Rate is the percentage of owners and lessees of new vehicles that receive our service and convert to become self-paying subscribers after an initial promotional period. The metric excludes rental and fleet vehicles. (See accompanying glossary on pages 39 through 41 for more details).
For the three months ended September 30, 2016 and 2015, our new vehicle consumer conversion rate was 40% and 41%, respectively. For the nine months ended September 30, 2016 and 2015, our new vehicle consumer conversion rate was 39% and 41%, respectively. The period over period decrease for the three and nine months ended September 30, 2016 was primarily due to an increased vehicle penetration rate as well as lower conversion of first-time buyers and lessees of satellite radio enabled cars.
ARPU is derived from total earned subscriber revenue (excluding revenue derived from our connected vehicle services), net advertising revenue and other subscription-related revenue, divided by the number of months in the period, divided by the daily weighted average number of subscribers for the period. (See the accompanying glossary on pages 39 through 41 for more details.)
For the three months ended September 30, 2016 and 2015, ARPU was $13.04 and $12.67, respectively. For the nine months ended September 30, 2016 and 2015, ARPU was $12.83 and $12.45, respectively. The period over period increase for the three and nine months ended September 30, 2016 was driven primarily by increases in certain of our subscription and other subscription-related rates, partially offset by growth in subscription discounts offered through customer acquisition and retention programs.
SAC, Per Installation, is derived from subscriber acquisition costs and margins from the sale of radios, components and accessories, divided by the number of satellite radio installations in new vehicles and shipments of aftermarket radios for the period. (See the accompanying glossary on pages 39 through 41 for more details.)
For the three months ended September 30, 2016 and 2015, SAC, per installation, was $28 and $34, respectively. For the nine months ended September 30, 2016 and 2015, SAC, per installation, was $31 and $33, respectively. The period over period decrease for the three months and nine months ended September 30, 2016 was driven by lower OEM hardware subsidy rates as well as lower subsidized costs related to the transition of chipsets. Additionally, for the three months ended September 30, 2016, subscriber acquisition costs benefited approximately $2.00 per installation from a contractual reduction to a subsidy rate.
Customer Service and Billing Expenses, Per Average Subscriber, is derived from total customer service and billing expenses, excluding connected vehicle customer service and billing expenses and share-based payment expense, divided by the number of months in the period, divided by the daily weighted average number of subscribers for the period. (See the accompanying glossary on pages 39 through 41 for more details.)
For the three months ended September 30, 2016 and 2015, customer service and billing expenses, per average subscriber, was $0.97 and $1.00, respectively. For the nine months ended September 30, 2016 and 2015, customer service and billing expenses, per average subscriber, was $0.98 and $1.00, respectively. The period over period decrease for the three months and nine months ended September 30, 2016 was primarily related to efficiencies achieved from call center process enhancements and lower personnel related costs, partially offset by increased bad debt expense and transaction fees per subscriber.
Adjusted EBITDA. EBITDA is defined as net income before interest expense, income tax expense and depreciation and amortization. Adjusted EBITDA excludes the impact of other income, other non-cash charges, such as certain purchase price accounting adjustments, share-based payment expense, and loss on disposal of assets and settlements related to the historical use of pre-1972 sound recordings. (See the accompanying glossary on pages 39 through 41 for a reconciliation to GAAP and for more details.)
For the three months ended September 30, 2016 and 2015, adjusted EBITDA was $491,892 and $447,194, respectively, an increase of 10%, or $44,698. For the nine months ended September 30, 2016 and 2015, adjusted EBITDA was $1,401,024 and $1,261,382, respectively, an increase of 11%, or $139,642. The increase was due to growth in revenues primarily as a result of the increase in our subscriber base and certain of our subscription rates, partially offset by higher revenue share and royalties costs due to growth in our revenues, higher programming and content costs associated with renewed agreements, higher sales and marketing costs associated with growth in our

subscriber base, and higher general and administrative costs.

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Free Cash Flow includes cash provided by operations, net of additions to property and equipment, and restricted and other investment activity, and excluding the $210,000 pre-1972 sound recordings legal settlement payment made in 2015. (See the accompanying glossary on pages 39 through 41 for a reconciliation to GAAP and for more details.)
For the three months ended September 30, 2016 and 2015, free cash flow was $356,527 and $368,899, respectively, a decrease of $12,372, or 3%. For the nine months ended September 30, 2016 and 2015, free cash flow was $1,079,690 and $1,016,045, respectively, an increase of $63,645 or 6%. The decrease for the three month period ended September 30, 2016 was driven by additions to property and equipment resulting primarily from new satellite construction, and a payment of approximately $22,400, net of insurance recoveries, in connection with the settlement of class action suits alleging violations of the Telephone Consumer Protection Act of 1991, partially offset by higher net cash provided by operating activities. The increase for the nine month period ended September 30, 2016 was primarily driven by higher net cash provided by operating activities resulting from higher collections from subscribers; partially offset by an increase in additions to property and equipment resulting primarily from new satellite construction and the payment of approximately $22,400, net of insurance recoveries, in connection with the settlement of class action suits alleging violations of the Telephone Consumer Protection Act of 1991.

Liquidity and Capital Resources

Cash Flows for the nine months ended September 30, 2016 compared with the nine months ended September 30, 2015

The following table presents a summary of our cash flow activity for the periods set forth below:

	For the Nine Months Ended September 30,		
	2016	2015	2016 vs 2015
Net cash provided by operating activities	$1,216,104	$900,954	$315,150
Net cash used in investing activities	(136,414)	(94,909)	(41,505)
Net cash used in financing activities	(619,146)	(801,224)	182,078
Net increase in cash and cash equivalents	460,544	4,821	455,723
Cash and cash equivalents at beginning of period	111,838	147,724	(35,886)
Cash and cash equivalents at end of period	$572,382	$152,545	$419,837

Cash Flows Provided by Operating Activities

Cash flows provided by operating activities increased by $315,150 to $1,216,104 for the nine months ended September 30, 2016 from $900,954 for the nine months ended September 30, 2015.

Our largest source of cash provided by operating activities is generated by subscription and subscription-related revenues. We also generate cash from the sale of advertising on certain non-music channels and the sale of satellite radios, components and accessories. Our primary uses of cash from operating activities include revenue share and royalty payments to distributors, programming and content providers, and payments to radio manufacturers, distributors and automakers. In addition, uses of cash from operating activities include payments to vendors to service, maintain and acquire subscribers, general corporate expenditures, and compensation and related costs.

Cash Flows Used in Investing Activities

Cash flows used in investing activities are primarily additional spending to construct replacement satellites, improve our terrestrial repeater network and for capitalized software. In 2015, our cash flows used in investing activities also included an increase to our letters of credit issued for the benefit of lessors of certain of our office space.

Cash Flows Used in Financing Activities

Cash flows used in financing activities consists of the issuance and repayment of long-term debt, cash used in our stock option program and the purchase of common stock under our share repurchase program. Proceeds from long-term debt, related party debt and equity issuances have been used to fund our operations, construct and launch new satellites and invest in other infrastructure improvements.

Cash flows provided by financing activities in the nine months ended September 30, 2016 were due to the issuance of $1,000,000 aggregate principal amount of 5.375% Senior Notes due 2026 and borrowings under the Credit Facility.
Cash flows used in financing activities in the nine months ended September 30, 2016 were primarily due to the purchase and

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retirement of shares of our common stock under our repurchase program for $1,225,284 and repayments of borrowings under the Credit Facility. Cash flows provided by financing activities in the nine months ended September 30, 2015 were due to the issuance of $1,000,000 aggregate principal amount of 5.375% Senior Notes due 2025 and borrowings under the Credit Facility. Cash flows used in financing activities in the nine months ended September 30, 2015 were primarily due to the purchase and retirement of shares of our common stock under our repurchase program for $1,647,728 and repayments of borrowings under the Credit Facility.

Future Liquidity and Capital Resource Requirements

Based upon our current business plans, we expect to fund operating expenses, capital expenditures, including the construction of replacement satellites, working capital requirements, legal settlements, interest payments, taxes and scheduled maturities of our debt with existing cash, cash flow from operations and borrowings under our Credit Facility. As of September 30, 2016, $1,750,000 was available for future borrowing under our Credit Facility. On October 3, 2016, we redeemed $650,000 in principal amount of our outstanding 5.875% Notes for an approximate purchase price of $669,097, including premium. This redemption was funded with $359,097 of Cash and cash equivalents and $310,000 of borrowings under our Credit Facility. We believe that we have sufficient cash and cash equivalents as well as debt capacity to cover our estimated short-term and long-term funding needs, as well as fund stock repurchases and strategic opportunities.

Our ability to meet our debt and other obligations depends on our future operating performance and on economic, financial, competitive and other factors. We continually review our operations for opportunities to adjust the timing of expenditures to ensure that sufficient resources are maintained.

We regularly evaluate our business plans and strategy. These evaluations often result in changes to our business plans and strategy, some of which may be material and significantly change our cash requirements. These changes in our business plans or strategy may include: the acquisition of unique or compelling programming; the development and introduction of new features or services; significant new or enhanced distribution arrangements; investments in infrastructure, such as satellites, equipment or radio spectrum; and acquisitions, including acquisitions that are not directly related to our satellite radio business.

Capital Return Program

As of September 30, 2016, our board of directors had approved for repurchase an aggregate of $8,000,000 of our common stock. As of September 30, 2016, our cumulative repurchases since December 2012 under our stock repurchase program totaled 2,098,548 shares for $7,515,223, and $484,777 remained available under our stock repurchase program.

On October 26, 2016, our board of directors approved an additional $2,000,000 for repurchase of our common stock. The new approval increases the amount of common stock that we have been authorized to repurchase to an aggregate of $10,000,000. Shares of common stock may be purchased from time to time on the open market and in privately negotiated transactions, including in accelerated stock repurchase transactions and transactions with Liberty Media and its affiliates. We intend to fund the additional repurchases through a combination of cash on hand, cash generated by operations and future borrowings.

On October 26, 2016, our board of directors also declared the first quarterly dividend on our common stock in the amount of $0.01 per share of common stock payable on November 30, 2016 to stockholders of record as of the close of business on November 9, 2016. Our board of directors expects that this dividend will be the first of regular quarterly dividends, in an aggregate annual amount of $0.04 per share of common stock.

Debt Covenants

The indentures governing Sirius XM's senior notes, and the agreement governing the Credit Facility include restrictive covenants. As of September 30, 2016, we were in compliance with such covenants. For a discussion of our “Debt Covenants,” refer to Note 10 to our unaudited consolidated financial statements in Item 1 of this Quarterly Report on Form 10-Q.

Off-Balance Sheet Arrangements

We do not have any significant off-balance sheet arrangements other than those disclosed in Note 13 to our unaudited consolidated financial statements in Item 1 of this Quarterly Report on Form 10-Q that are reasonably likely to have a material effect on our financial condition, results of operations, liquidity, capital expenditures or capital resources.

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Contractual Cash Commitments

For a discussion of our “Contractual Cash Commitments,” refer to Note 13 to our unaudited consolidated financial statements in Item 1 of this Quarterly Report on Form 10-Q.

Related Party Transactions

For a discussion of “Related Party Transactions,” refer to Note 9 to our unaudited consolidated financial statements in Item 1 of this Quarterly Report on Form 10-Q.

Critical Accounting Policies and Estimates

For a discussion of our “Critical Accounting Policies and Estimates,” refer to “Management's Discussion and Analysis of Financial Condition and Results of Operations” in our Annual Report on Form 10-K for the year ended December 31, 2015. There have been no material changes to our critical accounting policies and estimates since December 31, 2015.

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Adjusted EBITDA - EBITDA is defined as net income before interest expense, income tax expense and depreciation and amortization. We adjust EBITDA to exclude the impact of other income as well as certain other charges discussed below. Adjusted EBITDA is one of the primary Non-GAAP financial measures we use to (i) evaluate the performance of our on-going core operating results period over period, (ii) base our internal budgets and (iii) compensate management. Adjusted EBITDA is a Non-GAAP financial measure that excludes (if applicable): (i) certain adjustments as a result of the purchase price accounting for the Merger, (ii) share-based payment expense and (iii) other significant operating expense (income) that do not relate to the on-going performance of our business. We believe adjusted EBITDA is a useful measure of the underlying trend of our operating performance, which provides useful information about our business apart from the costs associated with our capital structure and purchase price accounting. We believe investors find this Non-GAAP financial measure useful when analyzing our results and comparing our operating performance to the performance of other communications, entertainment and media companies. We believe investors use adjusted EBITDA to estimate our current enterprise value and to make investment decisions. Because of large capital investments in our satellite radio system our results of operations reflect significant charges for depreciation expense. We believe the exclusion of share-based payment expense is useful as it is not directly related to the operational conditions of our business. We also believe the exclusion of settlements related to the historical use of pre-1972 sound recordings and loss on disposal of assets is useful as it does not represent an expense incurred as part of our normal operations for the period.

Adjusted EBITDA has certain limitations in that it does not take into account the impact to our statements of comprehensive income of certain expenses, including share-based payment expense and certain purchase price accounting for the Merger. We endeavor to compensate for the limitations of the Non-GAAP measure presented by also providing the comparable GAAP measure with equal or greater prominence and descriptions of the reconciling items, including quantifying such items, to derive the Non-GAAP measure. Investors that wish to compare and evaluate our operating results after giving effect for these costs, should refer to net income as disclosed in our unaudited consolidated statements of comprehensive income. Since adjusted EBITDA is a Non-GAAP financial performance measure, our calculation of adjusted EBITDA may be susceptible to varying calculations; may not be comparable to other similarly titled measures of other companies; and should not be considered in isolation, as a substitute for, or superior to measures of financial performance prepared in accordance with GAAP. The reconciliation of net income to the adjusted EBITDA is calculated as follows:

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2016	2015	2016	2015
Net income:	$193,901	$166,550	$541,306	$375,091
Add back items excluded from Adjusted EBITDA:				
Purchase price accounting adjustments:				
Revenues	1,813	1,813	5,438	5,438
Operating expenses	—	—	—	(1,394)
Pre-1972 sounds recordings legal settlements	—	—	—	107,658
Loss on disposal of assets	—	—	12,912	—
Share-based payment expense	30,020	23,393	77,890	62,334
Depreciation and amortization	67,880	70,404	202,215	202,527
Interest expense	89,092	76,624	250,888	221,912
Other income	(2,370)	(4,133)	(15,733)	(9,077)
Income tax expense	111,556	112,543	326,108	296,893
Adjusted EBITDA	$491,892	$447,194	$1,401,024	$1,261,382

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ARPU - is derived from total earned subscriber revenue, advertising revenue and other subscription-related revenue, excluding revenue associated with our connected vehicle services, divided by the number of months in the period, divided by the daily weighted average number of subscribers for the period. Other subscription-related revenue includes the U.S. Music Royalty Fee. ARPU is calculated as follows:

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2016	2015	2016	2015
Subscriber revenue, excluding connected vehicle	$1,048,033	$949,301	$3,044,438	$2,752,993
Add: advertising revenue	34,268	33,131	99,330	88,843
Add: other subscription-related revenue	122,013	106,483	353,606	299,437
	$1,204,314	$1,088,915	$3,497,374	$3,141,273
Daily weighted average number of subscribers	30,776	28,649	30,290	28,033
ARPU	$13.04	$12.67	$12.83	$12.45

Average self-pay monthly churn - is defined as the monthly average of self-pay deactivations for the period divided by the average number of self-pay subscribers for the period.

Customer service and billing expenses, per average subscriber - is derived from total customer service and billing expenses, excluding connected vehicle customer service and billing expenses and share-based payment expense, divided by the number of months in the period, divided by the daily weighted average number of subscribers for the period. We believe the exclusion of share-based payment expense in our calculation of customer service and billing expenses, per average subscriber, is useful as share-based payment expense is not directly related to the operational conditions that give rise to variations in the components of our customer service and billing expenses. Customer service and billing expenses, per average subscriber, is calculated as follows:

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2016	2015	2016	2015
Customer service and billing expenses, excluding connected vehicle	$90,582	$86,840	$270,964	$255,105
Less: share-based payment expense	(1,069)	(793)	(2,694)	(2,164)
	$89,513	$86,047	$268,270	$252,941
Daily weighted average number of subscribers	30,776	28,649	30,290	28,033
Customer service and billing expenses, per average subscriber	$0.97	$1.00	$0.98	$1.00

Free cash flow - is derived from cash flow provided by operating activities, net of additions to property and equipment, restricted and other investment activity and the return of capital from investment in unconsolidated entity. Free cash flow is a metric that our management and board of directors use to evaluate the cash generated by our operations, net of capital expenditures and other investment activity and significant items that do not relate to the on-going performance of our business. In a capital intensive business, with significant investments in satellites, we look at our operating cash flow, net of these investing cash outflows, to determine cash available for future subscriber acquisition and capital expenditures, to repurchase or retire debt, to acquire other companies and to evaluate our ability to return capital to stockholders. We believe free cash flow is an indicator of the long-term financial stability of our business. Free cash flow, which is reconciled to "Net cash provided by operating activities," is a Non-GAAP financial measure. This measure can be calculated by deducting amounts under the captions "Additions to property and equipment" and deducting or adding Restricted and other investment activity from "Net cash provided by operating activities" from the unaudited consolidated statements of cash flows, adjusted for any significant legal settlements. We have excluded the $210,000 payment related to the pre-1972 sound recordings legal settlement from our free cash flow calculation in the three and nine months ended September 30, 2015. Free cash flow should be used in conjunction with other GAAP financial performance measures and may not be comparable to free cash flow measures presented by other companies. Free cash flow should be viewed as a supplemental measure rather than an alternative measure of cash flows from operating activities, as determined in accordance with GAAP. Free cash flow is limited and does not represent remaining cash flows available for discretionary expenditures due to the fact that the measure does not deduct the payments required for debt maturities. We believe free cash flow provides useful supplemental information to investors regarding our current cash flow, along with other GAAP measures (such as cash flows from operating and investing activities), to determine our financial condition, and to compare our operating performance to other communications, entertainment and media companies. Free cash flow is calculated as follows:

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2016	2015	2016	2015
Cash Flow information				
Net cash provided by operating activities	$421,816	$188,613	$1,216,104	$900,954
Net cash used in investing activities	$(65,289)	$(29,714)	$(136,414)	$(94,909)
Net cash used in financing activities	$(260,598)	$(300,407)	$(619,146)	$(801,224)
Free Cash Flow				
Net cash provided by operating activities	$421,816	$188,613	$1,216,104	$900,954
Additions to property and equipment	(65,074)	(29,714)	(132,246)	(90,943)
Purchases of restricted and other investments	(215)	—	(4,168)	(3,966)
Pre-1972 sound recordings legal settlement	—	210,000	—	210,000
Free cash flow	$356,527	$368,899	$1,079,690	$1,016,045

New vehicle consumer conversion rate - is defined as the percentage of owners and lessees of new vehicles that receive our satellite radio service and convert to become self-paying subscribers after the initial promotion period. At the time satellite radio enabled vehicles are sold or leased, the owners or lessees generally receive trial subscriptions ranging from three to twelve months. We measure conversion rate three months after the period in which the trial service ends. The metric excludes rental and fleet vehicles.

Subscriber acquisition cost, per installation - or SAC, per installation, is derived from subscriber acquisition costs and margins from the sale of radios and accessories, divided by the number of satellite radio installations in new vehicles and shipments of aftermarket radios for the period. SAC, per installation, is calculated as follows:

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2016	2015	2016	2015
Subscriber acquisition costs	$120,111	$133,009	$381,516	$391,773
Less: margin from sales of radios and accessories	(21,632)	(16,629)	(57,104)	(50,958)
	$98,479	$116,380	$324,412	$340,815

Installations	3,498	3,429	10,404	10,305
SAC, per installation	$28	$34	$31	$33

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ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISKS

As of September 30, 2016, we did not hold or issue any free-standing derivatives. We hold investments in money market funds and certificates of deposit. These securities are consistent with the objectives contained within our investment policy. The basic objectives of our investment policy are the preservation of capital, maintaining sufficient liquidity to meet operating requirements and maximizing yield.

Our debt includes fixed rate instruments and the fair market value of our debt is sensitive to changes in interest rates. Sirius XM's borrowings under the Credit Facility carry a variable interest rate based on LIBOR plus an applicable rate based on its debt to operating cash flow ratio. We currently do not use interest rate derivative instruments to manage our exposure to interest rate fluctuations.

ITEM 4. CONTROLS AND PROCEDURES

Controls and Procedures

We maintain a set of disclosure controls and procedures designed to ensure that information required to be disclosed in reports that we file or submit under the Exchange Act of 1934, is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms. The design of any disclosure controls and procedures is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Any controls and procedures, no matter how well designed and operated, can provide only reasonable, not absolute, assurance of achieving the desired control objectives.

As of September 30, 2016, an evaluation was performed under the supervision and with the participation of our management, including James E. Meyer, our Chief Executive Officer, and David J. Frear, our Senior Executive Vice President and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures (as that term is defined in Rule 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934). Based on that evaluation, our management, including our Chief Executive Officer and our Chief Financial Officer, concluded that our disclosure controls and procedures were effective as of September 30, 2016.

There has been no change in our internal control over financial reporting (as that term is defined in Rule 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934) during the quarter ended September 30, 2016 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

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PART II — OTHER INFORMATION
ITEM 1. LEGAL PROCEEDINGS
In the ordinary course of business, we are a defendant or party to various claims and lawsuits, including those discussed below.
Telephone Consumer Protection Act Suits. We are a defendant in several purported class action suits that allege that we, or call center vendors acting on our behalf, made calls which violate provisions of the Telephone Consumer Protection Act of 1991 (the "TCPA"). The plaintiffs in these actions allege, among other things, that we called mobile phones using an automatic telephone dialing system without the consumer's prior consent or, alternatively, after the consumer revoked his or her prior consent. In one of the actions, the plaintiff also alleges that we violated the TCPA's call time restrictions and, in one of the other actions, the plaintiff, also alleges that we violated the TCPA's do not call restrictions. These purported class action cases are titled Erik Knutson v. Sirius XM Radio Inc., No. 12-cv-0418-AJB-NLS (S.D. Cal.), Francis W. Hooker v. Sirius XM Radio Inc., No. 4:13-cv-3 (E.D. Va.), Yefim Elikman v. Sirius XM Radio Inc. and Career Horizons, Inc., No. 1:15-cv-02093 (N.D. Ill.), and Anthony Parker v. Sirius XM Radio Inc., No. 8:15-cv-01710-JSM-EAJ (M.D. Fla), and are described in Item 3., Legal Proceedings, in our Annual Report on Form 10-K for the year ended December 31, 2015.
We have entered into an agreement to settle these purported class action suits. The settlement is expected to resolve the claims of consumers beginning in February 2008 relating to telemarketing calls to their mobile telephones. As part of this settlement, we have made a $35 million payment to a settlement fund (from which notice, administration and other costs and attorneys' fees will be paid), and are offering participating class members the option of receiving three months of our Select service for no charge, and will enter into agreements to make modifications to the practices of certain call center vendors. The settlement is subject to final court approval, which cannot be assured.
Pre-1972 Sound Recording Matters. In August 2013, SoundExchange, Inc. filed a complaint in the United States District Court for the District of Columbia alleging that we underpaid royalties for statutory licenses during the 2007-2012 period in violation of the regulations established by the Copyright Royalty Board for that period. SoundExchange principally alleges that we improperly reduced our calculation of gross revenues, on which the royalty payments are based, by deducting non-recognized revenue attributable to pre-1972 recordings and Premier package revenue that is not "separately charged" as required by the regulations. SoundExchange is seeking compensatory damages of not less than $50 million and up to $100 million or more, payment of late fees and interest, and attorneys' fees and costs.
In August 2014, the United States District Court for the District of Columbia granted our motion to dismiss the complaint without prejudice on the grounds that the case properly should be pursued before the Copyright Royalty Board rather than the district court. In December 2014, SoundExchange filed a petition with the Copyright Royalty Board requesting an order interpreting the applicable regulations. We have submitted legal briefs and other evidence supporting our position that our payments and practices complied with the regulations established by the Copyright Royalty Board for statutory licenses during the 2007-2012 period or, in the event that the Judges should find that the applicable regulations were unclear, that the Judges should clarify the regulations and confirm that our payments and practices complied with the regulations for that period. Briefing in this matter is complete and a decision from the Copyright Royalty Board is pending.
This matter is titled SoundExchange, Inc. v. Sirius XM Radio, Inc., No.13-cv-1290-RJL (D.D.C.), and Determination of Rates and Terms for Preexisting Subscription Services and Satellite Digital Audio Radio Services, United States Copyright Royalty Board, No. 2006-1 CRB DSTRA. Information concerning the action is publicly available in filings under the docket numbers. The outcome of this matter is inherently unpredictable and subject to significant uncertainties, many of which are beyond our control. No provision was made for losses to the extent such are not probable and estimable. We believe we have substantial defenses to the claims asserted, and intend to defend this action vigorously.
Other Matters. In the ordinary course of business, we are a defendant in various other lawsuits and arbitration proceedings, including derivative actions; actions filed by subscribers, both on behalf of themselves and on a class action basis; former employees; parties to contracts or leases; and owners of patents, trademarks, copyrights or other intellectual property. None of these other matters, in our opinion, is likely to have a material adverse effect on our

business, financial condition or results of operations.

ITEM 1A. RISK FACTORS

There have been no material changes to the risk factors previously disclosed in response to Part 1, Item 1A, of our Annual Report on Form 10-K for the year ended December 31, 2015.

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

As of September 30, 2016, our board of directors had approved for repurchase an aggregate of $8.0 billion of our common stock. On October 26, 2016, our board of directors approved an additional $2.0 billion for repurchase of our common stock. Our board of directors did not establish an end date for this stock repurchase program. Shares of common stock may be purchased from time to time on the open market, pursuant to pre-set trading plans meeting the requirements of Rule 10b5-1 under the Exchange Act, in privately negotiated transactions, including transactions with Liberty Media and its affiliates, or otherwise. As of September 30, 2016, our cumulative repurchases since December 2012 under our stock repurchase program totaled 2.1 billion shares for $7.5 billion, and $0.5 billion remained available under our stock repurchase program. The size and timing of these purchases will be based on a number of factors, including price and business and market conditions.

The following table provides information about our purchases of equity securities registered pursuant to Section 12 of the Securities Exchange Act of 1934, as amended, during the quarter ended September 30, 2016:

Period	Total Number of Shares Purchased	Average Price Paid Per Share (a)	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs (a)
July 1, 2016 - July 31, 2016	12,179,019	$ 4.07	12,179,019	$657,911,907
August 1, 2016 - August 31, 2016	19,893,860	$ 4.20	19,893,860	$574,297,398
September 1, 2016 - September 30, 2016	21,527,629	$ 4.16	21,527,629	$484,776,920
Total	53,600,508	$ 4.16	53,600,508	

(a) These amounts include fees and commissions associated with the shares repurchased.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not applicable.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS

See Exhibit Index attached hereto, which is incorporated herein by reference.

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SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) 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 on this 27th day of October 2016.

SIRIUS XM HOLDINGS INC.

By: /s/ DAVID J. FREAR
David J. Frear
Senior Executive Vice President and
Chief Financial Officer
(Principal Financial Officer)

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EXHIBIT INDEX

Exhibit	Description
31.1	Certificate of James E. Meyer, Chief Executive Officer, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).
31.2	Certificate of David J. Frear, Senior Executive Vice President and Chief Financial Officer, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).
32.1	Certificate of James E. Meyer, Chief Executive Officer, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (furnished herewith).
32.2	Certificate of David J. Frear, Senior Executive Vice President 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 (furnished herewith).
101.1	The following financial information from our Quarterly Report on Form 10-Q for the quarter ended September 30, 2016 formatted in eXtensible Business Reporting Language (XBRL): (i) Consolidated Statements of Comprehensive Income (Unaudited) for the three and nine months ended September 30, 2016 and 2015; (ii) Consolidated Balance Sheets as of September 30, 2016 (Unaudited) and December 31, 2015; (iii) Consolidated Statements of Stockholders' (Deficit) Equity for the nine months ended September 30, 2016 (Unaudited); (iv) Consolidated Statements of Cash Flows (Unaudited) for the nine months ended September 30, 2016 and

2015; and
(v) Notes to
Consolidated
Financial
Statements
(Unaudited).

The agreements and other documents filed as exhibits to this report are not intended to provide factual information or other disclosure other than with respect to the terms of the agreements or other documents themselves, and you should not rely on them for that purpose. In particular, any representations and warranties made by us in these agreements or other documents were made solely within the specific context of the relevant agreement or document and may not describe the actual state of affairs as of the date they were made or at any other time.