



YumChina

2016 Annual Report





Micky Pant
CEO, Yum China

A LONG AND SUCCESSFUL TRACK RECORD OF DOING BUSINESS IN CHINA

Dear Stockholders,

2016 was a momentous year for Yum China. We successfully became an independent, publicly traded company while simultaneously improving our business performance and investing for future growth.

Yum China has a long and successful track record of doing business in China; we opened our first KFC in 1987 in Qian Men, Beijing. As the first international restaurant chain operator entering the China market following the reform and opening up policy, we benefited from the tremendous growth of the Chinese economy, and we believe we are an integral part of the community. Over the past three decades, we have built an unprecedented national presence.

In 2016, we delivered a same-store sales growth turnaround and met or exceeded key financial goals. Operating profit reached \$640 million, an increase of 31% year-over-year, led by margin expansion and new store openings. Net income increased 55% year-over-year to \$502 million. Our adjusted EBITDA was \$1.13 billion, growth of 19% year-over-year, excluding the impact of foreign currency exchange. Our full year restaurant margin was 15.3%, an increase of 2.7 percentage points versus 2015. With 575 new stores opened in the year, we passed the 7,500 store milestone for the first time in our history. In addition, we remodeled 791 stores and launched our first flagship Taco Bell in Shanghai. Our real estate in China ranks among the best in the world of Yum Brands. With over 75% of stores built or renovated in the past five years, we believe we are very well positioned to drive future growth.

Adjusted EBITDA excluding the impact of foreign currency exchange is a non-GAAP financial measure. For information regarding non-GAAP financial measures, and a reconciliation of Adjusted EBITDA to net income, the most directly comparably GAAP measure, see pages 59 and 63 of our Annual Report on Form 10-K.

KFC

3%
SAME-STORE SALES
GROWTH
IN **2016**

Under the leadership of Joey Wat, KFC, which accounted for about 80% of our operating profit in 2016, performed strongly. KFC added 323 new stores, and further remodeled 720 stores. KFC delivered same-store sales growth of 3%, reversing a three-year declining trend. 2016 operating profit grew 29% year-over-year to \$645 million; restaurant margin improved to 16.3%, up 3 percentage points versus 2015. Our turnaround strategy for KFC has clearly taken hold; we are pleased with our progress, and believe we are well positioned for the future.



This letter contains "forward-looking statements." We intend all forward-looking statements to be covered by the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Refer to page 2 of our Annual Report on Form 10-K for additional information.





PIZZA HUT

Pizza Hut Casual Dining is a powerhouse brand in China's casual dining market. In 2016, Pizza Hut Casual Dining built 178 new stores and remodeled a further 69 stores. Same-store sales declined by 7% during the year, though system sales showed an increase of 3% year-over-year, excluding the impact of foreign currency exchange. To restore same-store sales growth at Pizza Hut, which is a top priority for us, we have formulated an action plan with five key steps. We will focus on core products, menu simplification, brand integration, sustainable development and digital acceleration.

178

NEW RESTAURANT
OPENINGS
IN 2016



Five Key Steps to Restore Sales Growth



1

Focus on Core



2

Menu
Simplification



3

Brand Integration



4

Sustainable
Development



5

Digital Acceleration



Yum China is the first international restaurant chain operator entering China market following the reform and opening up policy.

OVER
7,500
RESTAURANTS
ACROSS
1,100 CITIES
IN CHINA

2016 was also a ground breaking year for Yum China in Digital and Delivery. Cashless payments accounted for about 30% of our company sales. Total delivery sales reached \$700 million, and we have the largest online presence among restaurant operators in China. Our loyalty program has over 80 million members between KFC and Pizza Hut, and ranked No.1 in the restaurant industry worldwide in terms of number of members. We see Digital and Delivery as a robust new growth engine that will drive the restaurant industry going forward, and we believe we are very well positioned to benefit from this secular growth trend.

We are committed to giving back to local communities through our community engagement efforts. Our “Kids Book Club” initiative at KFC has been very successful, under which we gave away 14 million children’s books in 2016. Our “One Yuan Donation” program has raised RMB150 million since 2008, providing nutritional meals to children in need. Our social responsibility programs have been tailored to key needs, such as the challenges faced by kids left behind with grandparents as their parents migrate to cities in search of better jobs.

On February 7, 2017, we announced that the Board of Directors authorized a \$300 million stock repurchase program. This demonstrated our commitment to return capital to stockholders.

2017 is the Year of Rooster, and it also marks the 30th anniversary of KFC in China. We are optimistic about the strength of our business and our growth trajectory ahead. We believe the majority of our restaurants in China are yet to be built. We believe we are well positioned to drive operating performance and generate high returns to our stockholders in the long run.

M Pant



Yum China Holdings, Inc.

**7100 Corporate Drive
Plano, Texas 75024
United States of America**

**16/F Two Grand Gateway
3 Hong Qiao Road,
Shanghai 200030
People's Republic of China**

March 17, 2017

Dear Fellow Stockholders:

We are pleased to invite you to attend the 2017 Annual Meeting of Stockholders of Yum China Holdings, Inc. The Annual Meeting will be held Friday, April 28, 2017, at 8:30 a.m. local time, at Mandarin Oriental Hong Kong, 5 Connaught Road, Central, Hong Kong.

The attached notice and proxy statement contain details of the business to be conducted at the Annual Meeting. In addition, the Company's 2016 annual report, which is being made available to you along with the proxy statement, contains information about the Company and its performance.

Your vote is important. We encourage you to vote promptly, whether or not you plan to attend the Annual Meeting. You may vote your shares over the Internet or via telephone. If you received a paper copy of the proxy materials, you may complete, sign, date and mail the proxy card in the postage-paid envelope provided.

If you plan to attend the meeting, you may also vote in person. If you hold your shares through a bank, broker or other nominee, you will be required to show the notice or voting instructions form you received from your bank, broker or other nominee or a copy of a statement (such as a brokerage statement) from your bank, broker or other nominee reflecting your stock ownership as of February 28, 2017 in order to be admitted to the meeting. All attendees must bring valid photo identification to gain admission to the meeting. Whether or not you attend the meeting, we encourage you to consider the matters presented in the proxy statement and vote as soon as possible.

Sincerely,

Micky Pant
Chief Executive Officer

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YUM CHINA HOLDINGS, INC.
NOTICE OF ANNUAL MEETING OF STOCKHOLDERS

- Time and Date:** 8:30 a.m. (local time) on Friday, April 28, 2017
- Place:** Mandarin Oriental Hong Kong, 5 Connaught Road, Central, Hong Kong
- Items of Business:**
- (1) To elect the three Class I director nominees named in the accompanying proxy statement to serve until the 2019 annual meeting of the Company's stockholders.
 - (2) To ratify the appointment of KPMG Huazhen LLP as the Company's independent auditor for 2017.
 - (3) To approve, on an advisory basis, the Company's named executive officer compensation.
 - (4) To approve, on an advisory basis, the frequency of the advisory vote to approve the Company's named executive officer compensation.
 - (5) To transact such other business as may properly come before the meeting or any adjournment or postponement thereof.
- Who Can Vote:** You can vote if you were a stockholder of record as of the close of business on February 28, 2017.
- How to Vote:** You may vote over the Internet or via telephone by following the instructions set forth in the accompanying proxy statement. If you received a paper copy of the proxy materials, you may also vote by completing, signing, dating and returning the proxy card. If you attend the annual meeting, you may vote in person. ***Your vote is important. Whether or not you plan to attend the annual meeting, please vote promptly.***
- Date of Mailing:** This notice, the accompanying proxy statement and the form of proxy are first being mailed to stockholders on or about March 17, 2017.

By Order of the Board of Directors,



Shella Ng
Chief Legal Officer and Corporate Secretary

PROXY STATEMENT

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PROXY STATEMENT SUMMARY

This summary highlights information contained elsewhere in this proxy statement. This summary does not contain all of the information that you should consider, and you should read the entire proxy statement carefully before voting.

Meeting Information

Date: April 28, 2017
Time: 8:30 a.m. (local time)
Record Date: February 28, 2017

Location: Mandarin Oriental Hong Kong
5 Connaught Road, Central
Hong Kong

How to Vote

Whether or not you plan to attend the annual meeting, please vote as promptly as possible using one of the following methods:

- Via **Internet** by following the instructions on www.proxyvote.com;
- Via **telephone** by calling 1 (800) 690-6903 (toll-free in the U.S.) and following the instructions provided by the recorded message; or
- Via **mail**, if you received your proxy materials by mail, by completing, signing, dating and mailing the proxy card in the postage-paid envelope provided.

If you hold your shares in the name of a bank, broker or other nominee, your ability to vote by telephone or the Internet depends on their voting processes. Please follow the directions of your bank, broker or other nominee carefully.

Items of Business

Proposal	Board Voting Recommendation	Page Reference
1. Election of Three Class I Director Nominees to Serve for a Two-Year Term	FOR each nominee	17
2. Ratification of the Appointment of KPMG Huazhen LLP as the Company's Independent Auditor for 2017	FOR	22
3. Advisory Vote on Named Executive Officer Compensation	FOR	23
4. Advisory Vote on the Frequency of the Advisory Vote on Named Executive Officer Compensation	for ONE YEAR	24

Company Overview

On October 31, 2016, Yum China Holdings, Inc., a Delaware corporation (the "**Company**," "**we**," "**us**" or "**our**"), was spun-off from Yum! Brands, Inc. ("**YUM**"), becoming an independent publicly traded company as a result of a pro rata distribution of the Company's common stock to shareholders of YUM. In this proxy statement, we refer to this transaction as the "**spin-off**." We have the exclusive right to operate and sub-license in mainland China the KFC concept, the leading quick-service restaurant brand in China in terms of system sales and number of restaurants, the Pizza Hut concept, the leading casual dining restaurant brand in China as measured by system sales and number of

restaurants, and the Taco Bell concept, which opened its first restaurant in China in 2016. We also own the Little Sheep and East Dawning concepts outright.

Summary Information Regarding Directors

The following table provides summary information about our directors, each of whom joined our board of directors (the “*Board of Directors*” or the “*Board*”) in 2016 in connection with the spin-off from YUM.

Name	Age	Class; Year Term Expires	Primary Occupation	Independent	Board Committee Membership as of March 17, 2017		
					A	C	G
Fred Hu (Chairman)	53	III – 2019	Chairman and founder of Primavera Capital Group	✓			CC
Muktesh “Micky” Pant	62	II – 2018	Chief Executive Officer of the Company				
Peter A. Bassi	67	I – 2017	Former Chairman of Yum! Restaurants International	✓	X		
Christian L. Campbell	66	III – 2019	Owner of Christian L. Campbell Consulting LLC				
Ed Yiu-Cheong Chan	54	I – 2017	Vice Chairman of Charoen Pokphand Group Company Limited	✓	X		
Edouard Etedgui	65	I – 2017	Non-Executive Chairman of Alliance Française, Hong Kong	✓			CC
Louis T. Hsieh	52	II – 2018	Senior Adviser to the Chief Executive Officer of New Oriental Education & Technology Group	✓			CC
Jonathan S. Linen	73	II – 2018	Former Vice Chairman of American Express Company	✓		X	X
Ruby Lu	46	III – 2019	Independent venture capitalist	✓	X		X
Zili Shao	57	III – 2019	Partner at King & Wood Mallesons—China	✓			

A – Audit Committee; C – Compensation Committee; G – Nominating and Governance Committee; CC – Committee Chair

Governance Highlights

The Board believes that good corporate governance is a critical factor in achieving business success and in fulfilling the Board’s responsibilities to stockholders. The Board believes that its principles and practices align management and stockholder interests. Highlights include:

- Independent non-executive Chairman
- 8 of 10 directors are independent
- Declassified Board to be effective as of the 2019 annual meeting of the Company’s stockholders
- Majority voting for directors and director resignation policy in uncontested elections
- Proxy access

- All directors attended the Board meetings and the meetings of the Board committees of which they were members held in 2016 following the spin-off
- Board access to senior management and independent advisors
- No hedging or other speculative trading of Company stock
- Directors with experience, qualifications and skills across a wide range of public and private companies
- Independent and non-management directors may generally not stand for re-election if that person has reached age 75
- Policy regarding resignation if any director retires, changes employers or otherwise experiences a significant change in professional roles and responsibilities
- Expectation that directors should own a meaningful number of shares of Company common stock and that a director will not sell any shares of Company common stock received as director compensation until at least 12 months following the director's retirement or departure from the Board

Where You Can Find Additional Information

Our website is located at www.yumchina.com/En. Although the information contained on or connected to our website is not part of this proxy statement, you can view additional information on our website, such as our 2016 annual report, the charters of our Board committees, our Corporate Governance Principles, our Code of Conduct and reports that we file with the Securities and Exchange Commission (the "**SEC**"). Copies of these documents may also be obtained free of charge by writing Yum China Holdings, Inc., 7100 Corporate Drive, Plano, Texas 75024, or Yum China Holdings, Inc., 16/F Two Grand Gateway, 3 Hong Qiao Road, Shanghai 200030 People's Republic of China, Attention: Corporate Secretary.

QUESTIONS AND ANSWERS ABOUT THE MEETING AND VOTING

The Board of Directors of Yum China Holdings, Inc. solicits the enclosed proxy for use at the 2017 annual meeting of the Company's stockholders (the "**Annual Meeting**") to be held at 8:30 a.m. (local time), on Friday, April 28, 2017, at Mandarin Oriental Hong Kong, 5 Connaught Road, Central, Hong Kong. This proxy statement contains information about the matters to be voted on at the Annual Meeting and the voting process, as well as information about our directors and most highly paid executive officers.

What is the purpose of the Annual Meeting?

At the Annual Meeting, stockholders will vote on several important Company matters. In addition, our management will report on the Company's performance over the last fiscal year and, following the meeting, respond to questions from stockholders.

Why am I receiving these materials?

You received these materials because our Board of Directors is soliciting your proxy to vote your shares at the Annual Meeting. As a stockholder of record as of the close of business on February 28, 2017, you are invited to attend the Annual Meeting and are entitled to vote on the items of business described in this proxy statement.

Why did I receive a one-page notice in the mail regarding the Internet availability of proxy materials instead of a full set of proxy materials?

As permitted by SEC rules, we are making this proxy statement and our 2016 annual report available to our stockholders electronically via the Internet. On or about March 17, 2017, we mailed to our stockholders a Notice of Internet Availability of Proxy Materials (the "**Notice**") containing instructions on how to access this proxy statement and our 2016 annual report and vote online. If you received a Notice by mail, you will not receive a printed copy of the proxy materials unless you request a copy. The Notice contains instructions on how to access and review all of the important information contained in the proxy statement and the annual report. The Notice also instructs you on how you may submit your proxy over the Internet. If you received a Notice by mail and would like to receive a printed copy of our proxy materials, you should follow the instructions for requesting such materials contained on the Notice.

We encourage you to take advantage of the availability of the proxy materials on the Internet in order to help lower the costs of delivery and reduce the Company's environmental impact.

Who may attend the Annual Meeting?

The Annual Meeting is open to all stockholders of record as of the close of business on February 28, 2017, or their duly appointed proxies. If you would like to attend the Annual Meeting, you will need to bring a valid picture identification. If your shares are held in the name of a bank, broker or other nominee, you will need to bring a legal proxy from your bank or nominee or other proof of ownership as of the record date to be admitted to the Annual Meeting. A recent brokerage statement or letter from a bank, broker or other nominee is an example of proof of ownership.

Please note that computers, cameras, sound or video recording equipment, large bags, briefcases and packages will not be allowed in the meeting room.

May stockholders ask questions?

Yes. Representatives of the Company will answer stockholders' questions of general interest following the Annual Meeting.

Who may vote?

You may vote if you owned any shares of Company common stock as of the close of business on the record date, February 28, 2017. Each share of Company common stock is entitled to one vote. As of February 28, 2017, there were 384,311,143 shares of Company common stock outstanding.

What am I voting on?

You will be voting on the following five items of business at the Annual Meeting:

- The election of the three Class I director nominees named in this proxy statement to serve until the 2019 annual meeting of the Company's stockholders;
- The ratification of the appointment of KPMG Huazhen LLP as the Company's independent auditor for 2017;
- The approval, on an advisory basis, of the Company's named executive officer compensation; and
- The approval, on an advisory basis, of the frequency of the advisory vote to approve the Company's named executive officer compensation.

We will also consider other business that properly comes before the meeting.

How does the Board of Directors recommend that I vote?

Our Board of Directors recommends that you vote your shares:

- **FOR** each of the three nominees named in this proxy statement for election to the Board;
- **FOR** the ratification of the appointment of KPMG Huazhen LLP as our independent auditor for 2017;
- **FOR** the proposal regarding an advisory vote on named executive officer compensation; and
- **FOR** "one year" as the frequency of the non-binding advisory vote to approve named executive officer compensation.

How do I vote before the Annual Meeting?

There are three ways to vote before the meeting:

- By **Internet**—we encourage you to vote online at www.proxyvote.com by following instructions on the Notice or proxy card;
- By **telephone**—you may vote by making a telephone call to 1 (800) 690-6903 (toll free in the U.S.); or
- By **mail**—if you received your proxy materials by mail, you may vote by completing, signing, dating and mailing the proxy card in the postage-paid envelope provided.

Proxies submitted through the Internet or by telephone as described above must be received by 11:59 p.m., local time, on April 27, 2017. Proxies submitted by mail must be received prior to the meeting.

If you hold your shares in the name of a bank, broker or other nominee, your ability to vote by telephone or the Internet depends on their voting processes. Please follow the directions of your bank, broker or other nominee carefully.

Can I vote at the Annual Meeting?

Shares registered directly in your name as the stockholder of record may be voted in person at the Annual Meeting. Shares held through a bank, broker or other nominee may be voted in person only if you obtain a legal proxy from the bank, broker or other nominee that holds your shares giving you the right to vote the shares. Even if you plan to attend the Annual Meeting, we encourage you to vote your shares by proxy. You may still vote your shares in person at the meeting even if you have previously voted by proxy.

Can I change my mind after I vote?

You may change your vote at any time before the polls close at the Annual Meeting. You may do this by:

- signing another proxy card with a later date and returning it to us for receipt prior to the Annual Meeting;
- voting again by telephone or through the Internet prior to 11:59 p.m., local time, on April 27, 2017;
- giving written notice to the Corporate Secretary of the Company prior to the Annual Meeting; or
- voting again at the Annual Meeting.

Your attendance at the Annual Meeting will not have the effect of revoking a proxy unless you notify our Corporate Secretary in writing before the polls close that you wish to revoke a previous proxy.

Who will count the votes?

Representatives of American Stock Transfer and Trust Company, LLC will count the votes and will serve as the independent inspector of election.

What if I return my proxy card but do not provide voting instructions?

If you vote by proxy card, your shares will be voted as you instruct by the individuals named on the proxy card. If you sign and return a proxy card but do not specify how your shares are to be voted, the persons named as proxies on the proxy card will vote your shares in accordance with the recommendations of the Board set forth on page 1.

What does it mean if I receive more than one Notice or proxy card?

If you received more than one Notice or proxy card, it means that you have multiple accounts with brokers and/or our transfer agent. Please vote all of these shares. We recommend that you contact your broker and/or our transfer agent to consolidate as many accounts as possible under the same name and address. Our transfer agent is American Stock Transfer and Trust Company, LLC, which may be reached at 1 (888) 439-4986.

Will my shares be voted if I do not provide my proxy?

Your shares may be voted on certain matters if they are held in the name of a brokerage firm, even if you do not provide the brokerage firm with voting instructions. Brokerage firms have the authority under the New York Stock Exchange (“*NYSE*”) rules to vote shares for which their customers do not provide voting instructions on certain “routine” matters.

The proposal to ratify the appointment of KPMG Huazhen LLP as our independent auditor for 2017 is considered a routine matter for which brokerage firms may vote shares for which they have not received voting instructions. The other matters to be voted on at our Annual Meeting are not considered “routine” under applicable rules. When a matter is not a routine matter and the brokerage firm has not received voting instructions from the beneficial owner of the shares with respect to that matter, the brokerage firm cannot vote the shares on that proposal. This is called a “broker non-vote.”

How many votes must be present to hold the Annual Meeting?

Your shares are counted as present at the Annual Meeting if you attend the Annual Meeting in person or if you properly submit a proxy by Internet, telephone or mail. In order for us to conduct our Annual Meeting, a majority of the shares of Company common stock outstanding as of February 28, 2017 must be present in person or represented by proxy at the Annual Meeting. This is referred to as a “quorum.” Abstentions and broker non-votes will be counted for purposes of establishing a quorum at the Annual Meeting.

How many votes are needed to elect directors?

You may vote “FOR” each nominee or “AGAINST” each nominee, or “ABSTAIN” from voting on one or more nominees. Unless you mark “AGAINST” or “ABSTAIN” with respect to a particular nominee or nominees or for all nominees, your proxy will be voted “FOR” each of the director nominees named in this proxy statement. In an uncontested election, a nominee will be elected as a director if the number of “FOR” votes exceeds 50% of the number of votes cast with respect to that director’s election. Abstentions will be counted as present but not voted. Abstentions and broker non-votes will not affect the outcome of the election of directors. Full details of the Company’s majority voting policy are set out in our Corporate Governance Principles and are described on page 10 under “Governance of the Company-Majority Voting Policy.”

How many votes are needed to approve the other proposals?

Proposals 2 and 3 must receive the “FOR” vote of a majority of the shares, present in person or represented by proxy, and entitled to vote at the Annual Meeting. For each of these items, you may vote “FOR,” “AGAINST” or “ABSTAIN.” Abstentions will be counted as shares present and entitled to vote at the Annual Meeting. Accordingly, abstentions will have the same effect as a vote “AGAINST” Proposals 2 and 3. Broker non-votes will not be counted as shares present and entitled to vote with respect to the particular matter on which the broker has not voted. Thus, broker non-votes will not affect the outcome of any of these proposals.

For Proposal 4, you may vote for the option of “ONE YEAR,” “TWO YEARS,” “THREE YEARS” or “ABSTAIN.” The frequency that receives the highest number of votes cast will be the stockholders’ recommendation as to the frequency of future advisory votes to approve named executive officer compensation. Abstentions will be counted as present but not voted. Abstentions and broker non-votes will not affect the outcome of Proposal 4.

When will the Company announce the voting results?

The Company will announce the voting results of the Annual Meeting on a Current Report on Form 8-K filed with the SEC within four business days of the Annual Meeting.

What if other matters are presented for consideration at the Annual Meeting?

The Company knows of no other matters to be submitted to the stockholders at the Annual Meeting, other than the proposals referred to in this proxy statement. If any other matters properly come before the stockholders at the Annual Meeting, it is the intention of the persons named on the proxy to vote the shares represented thereby on such matters in accordance with their best judgment.

GOVERNANCE OF THE COMPANY

The business and affairs of the Company are managed under the direction of the Board of Directors. The Board believes that good corporate governance is a critical factor in achieving business success and in fulfilling the Board's responsibilities to stockholders. The Board believes that its practices align management and stockholder interests.

The corporate governance section of our website makes available certain of the Company's corporate governance materials, including our Corporate Governance Principles, the charters for each Board committee and our Code of Conduct. To access these documents on our Investor Relations website, *ir.yumchina.com*, click on "Governance" and then "Corporate Governance Documents."

Highlights of our corporate governance principles and practices are described below.

- Independent non-executive Chairman
- 8 of 10 directors are independent
- Declassified Board to be effective as of the 2019 annual meeting of the Company's stockholders
- Majority voting for directors and director resignation policy in uncontested elections
- Proxy access
- All directors attended the Board meetings and the meetings of the Board committees of which they were members held in 2016 following the spin-off
- Board access to senior management and independent advisors
- No hedging or other speculative trading of Company stock
- Directors with experience, qualifications and skills across a wide range of public and private companies
- Independent and non-management directors may generally not stand for re-election if that person has reached age 75
- Policy regarding resignation if any director retires, changes employers or otherwise experiences a significant change in professional roles and responsibilities
- Expectation that directors should own a meaningful number of shares of Company common stock and that a director will not sell any shares of Company common stock received as director compensation until at least 12 months following the director's retirement or departure from the Board

What is the composition of the Board of Directors and how often are members elected?

Our Board of Directors presently consists of ten directors. As discussed in more detail later in this section, the Board has determined that eight of those directors, including all three of the directors standing for election at the Annual Meeting, are independent under the rules of the NYSE.

The Board is currently divided into three classes of approximately equal size. The directors designated as Class I directors have terms expiring at the Annual Meeting. The directors designated as Class II directors have terms expiring at the 2018 annual meeting of the Company's stockholders, and the directors designated as Class III directors have terms expiring at the 2019 annual meeting of the Company's stockholders. Beginning at the 2019 annual meeting of the Company's stockholders, each of our directors will stand for election each year for an annual term, and our Board will therefore no longer be divided into three classes.

How often did the Board meet in 2016?

The Company became an independent publicly traded company on November 1, 2016. The Board of Directors met once during 2016 following the spin-off. All the directors attended that meeting of the Board and the meetings of the Board committees of which they were members and that were held during 2016 following the spin-off.

What is the Board's policy regarding director attendance at the Annual Meeting?

The Board of Director's policy is that all directors are encouraged to attend the Annual Meeting.

How are director nominees selected?

The Nominating and Governance Committee is responsible for recommending director candidates to the full Board for nomination and election at the annual meetings of stockholders. The Nominating and Governance Committee will interview a director candidate before the candidate is submitted to the full Board for approval. The Nominating and Governance Committee's charter provides that it may retain a third-party search firm to identify candidates from time to time. The Nominating and Governance Committee will also consider director candidates recommended by stockholders or other sources in the same manner as nominees identified by the Committee. For a stockholder to submit a candidate for consideration by the Nominating and Governance Committee, a stockholder must notify the Company's Corporate Secretary by mail at Yum China Holdings, Inc., 7100 Corporate Drive, Plano, Texas 75024 or at Yum China Holdings, Inc., 16/F Two Grand Gateway, 3 Hong Qiao Road, Shanghai 200030 People's Republic of China.

In accordance with the Corporate Governance Principles, our Board seeks members from diverse professional backgrounds who combine a broad spectrum of experience and expertise with a reputation for integrity. Directors should have experience in positions with a high degree of responsibility and be leaders in the companies or institutions with which they are affiliated, and are selected based upon contributions they can make to the Board and management. The Nominating and Governance Committee seeks to complete customary vetting procedures and background checks with respect to individuals suggested for potential Board membership by stockholders of the Company or other sources.

Each of our current directors joined the Board in connection with the spin-off from YUM following a search initiated by a committee of YUM's board of directors. None of the nominees nor any current Class II or Class III directors have been elected by our public stockholders.

We believe that each of our directors has met the guidelines set forth in the Corporate Governance Principles. As noted in the director biographies that follow this section, our directors have experience, qualifications and skills across a wide range of public and private companies, possessing a broad spectrum of experience both individually and collectively.

Can stockholders nominate directors for election to the Board?

Yes, under our amended and restated bylaws, stockholders may nominate persons for election as directors at an annual meeting by following the procedures described under "Additional Information."

In addition, our amended and restated bylaws include provisions permitting, subject to certain terms and conditions, stockholders owning at least 3% of the outstanding shares of Company common stock for at least three consecutive years to use our annual meeting proxy statement to nominate a number of director candidates not to exceed 20% of the number of directors in office, subject to reduction in certain circumstances. Because we have been an independent publicly traded company for less than three years, stockholders will not be able to nominate directors for election using these proxy access procedures until the 2020 annual meeting of the Company's stockholders.

What is the Board's leadership structure?

Our Board is currently led by an independent Chairman, Dr. Fred Hu. Our Board believes that Board independence and oversight of management are effectively maintained through a strong independent Chairman and through the

Board's composition, committee system and policy of having regular executive sessions of non-management directors, all of which are discussed below this section. Further, separating the Chairman and Chief Executive Officer roles enables the Chairman to focus on corporate governance matters and the Chief Executive Officer to focus on the Company's business. We find that this structure works well to foster an open dialogue and constructive feedback among the independent directors and management. It further allows the Board to effectively represent the best interests of all stockholders and contribute to the Company's long-term success.

To promote effective independent oversight, the Board has adopted a number of governance practices discussed below.

What are the Company's governance policies and ethical guidelines?

- **Board Committee Charters.** The Audit Committee, Compensation Committee and Nominating and Governance Committee of the Board of Directors operate pursuant to their respective written charters. These charters were approved by the Board of Directors and reflect certain best practices in corporate governance. These charters comply with the requirements of the NYSE. Each charter is available on the Company's website at *ir.yumchina.com*.
- **Governance Principles.** The Board of Directors has documented its corporate governance principles in the Yum China Holdings, Inc. Board of Directors Corporate Governance Principles. These principles are available on the Company's website at *ir.yumchina.com*.
- **Ethical Guidelines.** YUMC's Code of Conduct was adopted to emphasize the Company's commitment to the highest standards of business conduct. The Code of Conduct also sets forth information and procedures for employees to report ethical or accounting concerns, misconduct or violations of the Code of Conduct in a confidential manner. The Code of Conduct applies to all directors and employees of the Company, including the principal executive officer, the principal financial officer and the principal accounting officer. All employees of the Company are required, on an annual basis, to complete the Yum China Code of Conduct Questionnaire and certify in writing that they have read and understand the Code of Conduct. The Code of Conduct is available on the Company's website at *ir.yumchina.com*. The Company intends to post amendments to or waivers from the Code of Conduct (to the extent applicable to directors or executive officers) on this website.

What other significant Board practices does the Company have?

- **Executive Sessions.** Our independent and non-management directors meet regularly in executive session. The executive sessions are attended only by the independent and non-management directors and are presided over by the independent Chairman. Our independent directors also meet in executive session at least once per year.
- **Role of Lead Director.** Our Corporate Governance Principles require the independent directors to appoint a Lead Director when the Chairman does not qualify as independent in accordance with the applicable rules of the NYSE. The Company currently does not have a Lead Director because the Chairman of the Board is independent.
- **Advance Materials.** Information and data important to the directors' understanding of the business or matters to be considered at a Board or committee meeting are, to the extent practical, distributed to the directors sufficiently in advance of the meeting to allow careful review prior to the meeting.
- **Board and Committee Evaluations.** The Board will conduct an annual self-evaluation process that is led by the Nominating and Governance Committee. This assessment focuses on the Board's contribution to the Company and emphasizes those areas in which the Board believes a better contribution could be made. In addition, the Audit Committee, the Compensation Committee and the Nominating and Governance Committees also each conduct a similar annual self-evaluation.

- **Majority Voting Policy.** Our amended and restated bylaws require majority voting for the election of directors in uncontested elections. This means that director nominees in an uncontested election for directors must receive a number of votes “FOR” their election in excess of 50% of the number of votes cast with respect to that director’s election. The Corporate Governance Principles further provide that any incumbent director who does not receive a majority of “FOR” votes will promptly tender to the Board his or her resignation from the Board. The resignation will specify that it is effective upon the Board’s acceptance of the resignation. The Board will, through a process managed by the Nominating and Governance Committee and excluding the nominee in question, accept or reject the resignation and publicly disclose the Board’s decision regarding the resignation and the rationale behind the decision within 90 days from the date of the certification of the election results.
- **Access to Management and Employees.** Our directors have complete and open access to senior members of management. Our Chief Executive Officer invites key employees of the Company to attend Board sessions at which the Chief Executive Officer believes they can meaningfully contribute to Board discussion.
- **Access to Outside Advisors.** The Board and Board committees have the right to consult and retain independent legal and other advisors at the expense of the Company. The Audit Committee has the sole authority to appoint, determine funding for and replace the independent auditor. The Compensation Committee has the sole authority to retain any advisor to assist it in the performance of its duties, after taking into consideration all factors relevant to the advisor’s independence from management. The Nominating and Governance Committee has the sole authority to retain search firms to be used to identify director candidates.

What is the Board’s role in risk oversight?

The Board maintains overall responsibility for overseeing the Company’s risk management framework, including succession planning. In furtherance of its responsibility, the Board has delegated specific risk-related responsibilities to the Audit Committee and the Compensation Committee.

The Audit Committee engages in substantive discussions with management regarding the Company’s major risk exposures and the steps management has taken to monitor and control such exposures, including the Company’s risk assessment and risk management policies. Our Head of Corporate Audit reports directly to the Audit Committee, as well as our Chief Financial Officer. The Audit Committee also receives reports at each meeting regarding legal and regulatory risks from management and meets periodically in separate executive sessions with our independent auditor and our Head of Corporate Audit. The Audit Committee periodically provides a summary to the full Board of the risk area reviewed together with any other risk-related subjects discussed at the Audit Committee meeting. Alternatively, the Board may review and discuss directly with management the major risks arising from the Company’s business and operations.

The Compensation Committee considers the risks that may be implicated by our compensation programs through a risk assessment conducted by management and reports its conclusions to the full Board. This oversight helps ensure the Company’s compensation programs align with the Company’s goals and compensation philosophies and, along with other factors, operate to mitigate against the risk that such programs would encourage excessive or inappropriate risk-taking.

How does the Board determine which directors are considered independent?

The Company’s Corporate Governance Principles, adopted by the Board, require that a majority of the directors qualify as independent in accordance with the applicable rules of the NYSE. The Board determines on an annual basis whether each director qualifies as independent pursuant to the applicable rules of the NYSE.

Pursuant to the Corporate Governance Principles, the Board undertook its annual review of director independence. During this review, the Board considered transactions and relationships between each director or any member of his

or her immediate family and the Company and its subsidiaries and affiliates. As provided in the Corporate Governance Principles, the purpose of this review was to determine whether any such relationships or transactions were inconsistent with a determination that the director is independent.

As a result of the review, the Board affirmatively determined that all of the directors are independent of the Company and its management under NYSE rules, with the exception of Christian Campbell and Micky Pant. Messrs. Campbell and Pant are not considered independent directors because Mr. Campbell served as an executive officer of YUM until his retirement in February 2016, and Mr. Pant is our Chief Executive Officer.

In determining that the other directors did not have a material relationship with the Company, the Board determined that Dr. Hu, Messrs. Bassi, Chan, Ettetdgui, Hsieh, Linen and Shao and Ms. Lu had no other relationship with the Company other than their relationship as a director. The Board did note, as discussed in the next paragraph, that Mr. Shao is a Partner at King & Wood Mallesons—China, which has a business relationship with the Company; however, as noted below, the Board determined that this relationship was not material to Mr. Shao or King & Wood Mallesons—China, and therefore determined Mr. Shao was independent.

The Company paid King & Wood Mallesons—China, the law firm at which Mr. Shao serves as Partner, approximately \$270,000 for legal services rendered to the Company in 2016. Based on publicly available information regarding the revenue such firm generated in 2016, and based on the fact that Mr. Shao did not directly participate in rendering such services to the Company, the Board determined this relationship was not material to Mr. Shao or King & Wood Mallesons—China.

How do stockholders communicate with the Board?

Stockholders or other parties who wish to communicate directly with the non-management directors as a group or the entire Board may do so by writing to the Nominating and Governance Committee, c/o the Corporate Secretary, Yum China Holdings, Inc., 7100 Corporate Drive, Plano, Texas, 75024. The Nominating and Governance Committee of the Board has approved a process for handling letters received by the Company and addressed to non-management members of the Board or the entire Board. Under that process, the Corporate Secretary of the Company reviews all such correspondence and regularly forwards to a designated member of the Nominating and Governance Committee copies of all such correspondence (except commercial correspondence and correspondence that is duplicative in nature) and a summary of all such correspondence. Directors may at any time review a log of all correspondence received by the Company that is addressed to members of the Board and request copies of any such correspondence. Written correspondence from stockholders relating to accounting, internal controls or auditing matters are brought to the attention of the Chairperson of the Audit Committee and to the internal audit department and are handled in accordance with procedures established by the Audit Committee with respect to such matters (described below). Correspondence from stockholders relating to Compensation Committee matters are referred to the Chairperson of the Compensation Committee.

What are the Company's policies on reporting of concerns regarding accounting and auditing matters?

The Audit Committee has established policies on reporting concerns regarding accounting and auditing matters in addition to our policy on communicating with our non-management directors. Any employee may, on a confidential or anonymous basis, submit complaint or concerns regarding accounting or auditing matters to the Chief Legal Officer of the Company through the Company's Employee Hotline or by e-mail or regular mail. If an employee is uncomfortable for any reason contacting the Chief Legal Officer, the employee may contact the Chairperson of the Audit Committee. The Chief Legal Officer maintains a log of all complaints or concerns, tracking their receipt, investigation and resolution and prepares a periodic summary report thereof for the Audit Committee.

What are the Committees of the Board?

The Board of Directors has standing Audit, Compensation and Nominating and Governance Committees.

Name of Committee and Members	Functions of the Committee	Number of Meetings in 2016
Audit Committee Louis T. Hsieh, <i>Chair</i> Peter A. Bassi Ed Yiu-Cheong Chan Ruby Lu	<ul style="list-style-type: none">• Possesses sole authority regarding the selection and retention of the independent auditor• Reviews and has oversight over the Company's internal audit function• Reviews and approves all auditing services, internal control-related services and permitted non-audit services to be performed for the Company by the independent auditor• Reviews the independence, qualification and performance of the independent auditor• Reviews and discusses with management and the independent auditor any major issues as to the adequacy of the Company's internal controls, any special steps adopted in light of material control deficiencies and the adequacy of disclosures about changes in internal control over financial reporting• Reviews and discusses with management and the independent auditor the annual audited financial statements, results of the review of the Company's quarterly financial statements and significant financial reporting issues and judgments made in connection with the preparation of the Company's financial statements• Reviews the Company's accounting and financial reporting principles and practices, including any significant changes thereto• Advises the Board with respect to Company policies and procedures regarding compliance with applicable laws and regulations and with the Company's Code of Conduct• Discusses with management the Company's major risk exposures and the steps management has taken to monitor and control such exposures, including the Company's risk assessment and risk management policies. Further detail about the role of the Audit Committee in risk assessment and risk management is included in the section entitled "What is the Board's role in risk oversight?" set forth on page 11.	1

The Board of Directors has determined that all of the members of the Audit Committee are independent within the meaning of applicable SEC regulations and the listing standards of the NYSE and that Mr. Hsieh, the Chairperson of the Committee, is qualified as an audit committee financial expert within the meaning of SEC regulations. The Board has also determined that Mr. Hsieh has accounting and related financial management expertise within the meaning of the listing standards of the NYSE and that each member is financially literate within the meaning of the listing standards of the NYSE.

Name of Committee and Members	Functions of the Committee	Number of Meetings in 2016
Compensation Committee Edouard Ettetdgui, <i>Chair</i> Jonathan S. Linen	<ul style="list-style-type: none"> • Oversees the Company’s executive compensation plans and programs and reviews and recommends changes to these plans and programs • Monitors the performance of the Chief Executive Officer and other senior executives in light of corporate goals set by the Committee • Reviews and approves the corporate goals and objectives relevant to the Chief Executive Officer’s and other senior executives’ compensation and evaluates their performance in light of those goals and objectives • Determines and approves the compensation level of the Chief Executive Officer and other senior executive officers based on this evaluation • Reviews the Company’s compensation plans, policies and programs to assess the extent to which they encourage excessive or inappropriate risk-taking or earnings manipulation • Reviews management succession planning and makes recommendations to the Board 	1

The Board has determined that all of the members of the Compensation Committee are independent within the meaning of the listing standards of the NYSE.

Name of Committee and Members	Functions of the Committee	Number of Meetings in 2016
Nominating and Governance Committee Fred Hu, <i>Chair</i> Jonathan S. Linen Ruby Lu	<ul style="list-style-type: none"> • Identifies and proposes to the Board individuals qualified to become Board members and recommends to the Board director nominees for each committee • Advises the Board on matters of corporate governance • Reviews and reassesses from time to time the adequacy of the Company’s Corporate Governance Principles and recommends any proposed changes to the Board for approval • Receives comments from all directors and reports annually to the Board with assessment of the Board’s performance • Reviews annually and makes recommendations to the Board with respect to the compensation and benefits of directors 	1

The Board has determined that all of the members of the Nominating and Governance Committee are independent within the meaning of the listing standards of the NYSE.

What are the Company’s policies and procedures with respect to related person transactions?

Under the Company’s Related Person Transaction Policies and Procedures, the Audit Committee reviews the material facts of all related person transactions that require the Audit Committee’s approval and either approves or

disapproves of the entry into the related person transaction. In determining whether to approve or ratify a related person transaction, the Audit Committee will determine whether such transaction is in, or not opposed to, the best interest of the Company and will take into account, among other factors it deems appropriate, whether such transaction is on terms no less favorable to the Company than terms generally available to an unaffiliated third party under the same or similar circumstances and the extent of the related person's interest in the transaction. Transactions, arrangements or relationships or any series of similar transactions, arrangements or relationships in which (i) a related person has or will have a direct or indirect material interest, (ii) the Company is a participant and (iii) that exceed \$120,000 in any calendar year are subject to the Audit Committee's review. Any director who is a related person with respect to a transaction under review may not participate in any discussion or approval of the transaction, except that the director will provide all material information concerning the transaction to the Audit Committee.

Related persons are directors, director nominees, executive officers, beneficial owners of 5% or more of the outstanding shares of Company common stock and their immediate family members. An immediate family member includes a person's children, stepchildren, parents, stepparents, spouse, siblings, mothers- and fathers-in-law, sons- and daughters-in-law, and brothers- and sisters-in-law and anyone sharing such person's household (other than a tenant or employee).

After its review, the Audit Committee may approve or ratify the transaction. The policies and procedures provide that certain transactions are deemed to be pre-approved even if they will exceed \$120,000. These transactions include employment of executive officers, director compensation and transactions with other companies if the aggregate amount of the transaction does not exceed the greater of \$1 million or 2% of that company's total consolidated gross revenues and the related person is not an executive officer of the other company.

Other than as described below, there were no transactions considered to be a related person transaction from November 1, 2016, the date on which the Company became an independent publicly traded company, through the date of this proxy statement.

In connection with the spin-off, on September 1, 2016, YUM and the Company entered into investment agreements with each of Pollos Investment L.P., an affiliate of Primavera Capital Group ("Primavera"), and API (Hong Kong) Investment Limited, an affiliate of Zhejiang Ant Small and Micro Financial Services Group Co., Ltd. ("Ant Financial" and, together with Primavera, the "Investors"). Pursuant to the investment agreements, on November 1, 2016, Primavera and Ant Financial collectively invested \$460 million (the "Investment") in the Company in exchange for: (i) shares of the Company's common stock representing in the aggregate 4.8% of the Company's common stock issued and outstanding immediately following the spin-off, after giving effect to the post-closing adjustment as discussed below and (ii) two tranches of warrants (the "Warrants"), exercisable by the Investors for an approximate additional 3.9% ownership, in the aggregate, of the Company's common stock issued and outstanding after the spin-off, taking into account the shares previously issued to the Investors. In connection with and at the closing of the Investment, on November 1, 2016, the Company and the Investors entered into a shareholders agreement, relating to rights and obligations of the Investors as holders of Company common stock and Warrants. Pursuant to the terms of the shareholders agreement, Primavera designated one member of the Board, Dr. Hu, and one non-voting Board observer. In addition, Ant Financial designated one non-voting Board observer.

On January 9, 2017, following the expiration of the post-closing measurement period specified in the investment agreements, the Company repurchased from the Investors a portion of the previously-issued shares of Company common stock at par value. In addition, the Company issued the Warrants to the Investors. These transactions were completed pursuant to the terms of the investment agreements entered into prior to the spin-off and were, accordingly, approved by the board of directors of YUM.

Does the Company require stock ownership by directors?

The Board believes that the number of shares of Company common stock owned by each director is a personal decision. However, the Board strongly supports the position that directors should own a meaningful number of shares of Company common stock and expects that a director will not sell any shares received as director compensation until at least 12 months following the director's retirement or departure from the Board.

The Company's non-employee directors receive a significant portion of their annual compensation in shares of Company common stock. The Company believes that the emphasis on the equity component of director compensation serves to further align the interests of directors with those of our stockholders.

How many shares of Company common stock do the directors own?

Stock ownership information for each director is shown in the table on page 25.

How are directors compensated?

Employee directors do not receive additional compensation for serving on the Board of Directors. The annual compensation for each director who is not an employee of the Company is discussed under "2016 Director Compensation" beginning on page 50.

MATTERS REQUIRING STOCKHOLDER ACTION

Item 1. Election of Directors

On November 1, 2016, YUM distributed all of the issued and outstanding shares of Company common stock to YUM stockholders. As a result, the Company became an independent, publicly traded company. Each of our current directors joined the Board in connection with the spin-off.

The Board is currently divided into three classes of approximately equal size. The directors designated as Class I directors have terms expiring at the Annual Meeting. The directors designated as Class II directors have terms expiring at the 2018 annual meeting of the Company's stockholders, and the directors designated as Class III directors have terms expiring at the 2019 annual meeting of the Company's stockholders. Directors elected to succeed Class I, II and III directors whose terms then expire will be elected for a term of office that expires at the 2019 annual meeting of the Company's stockholders. Beginning at the 2019 annual meeting of the Company's stockholders, each of our directors will stand for election each year for an annual term, and our Board will therefore no longer be divided into three classes.

Who are the Class I director nominees?

The Board has selected Peter A. Bassi, Ed Yiu-Cheong Chan and Edouard Ettegui for election as Class I director nominees. None of the Class I nominees has been elected by our public stockholders. If elected, the nominees will serve as directors and hold office until the 2019 annual meeting of the Company's stockholders and until their respective successors have been duly elected and qualified or until their earlier death, resignation or removal.

The biographies of each of the nominees for Class I directors and the continuing Class II and Class III directors below contain information regarding the person's service as a director, business experience, director positions held currently or at any time during the last five years, information regarding involvement in certain legal or administrative proceedings, if applicable, and the experiences, qualifications, attributes or skills that caused the Nominating and Governance Committee and the Board to determine that the person should serve as a director for the Company. In addition to the information presented below regarding each nominee's specific experience, qualifications, attributes and skills that led our Board to the conclusion that he or she should serve as a director, we also believe that all of our director nominees have a reputation for integrity, honesty and adherence to high ethical standards. They each have demonstrated business acumen and an ability to exercise sound judgment, as well as a commitment of service to the Company and our Board.

There are no family relationships among any of the directors and executive officers of the Company. Director ages are as of February 28, 2017.

What if a nominee is unwilling or unable to serve?

That is not expected to occur. If it does, proxies may be voted for a substitute nominated by the Board of Directors.

What vote is required to elect directors?

A nominee will be elected as a director if the number of "FOR" votes exceeds the number of "AGAINST" votes with respect to his election.

The Board of Directors recommends that you vote FOR the election of the three Class I director nominees.

Nominees for Class I Directors Whose Terms Will Expire in 2017



Peter A. Bassi

Age 67

Director Since 2016

Peter A. Bassi served as Chairman of Yum! Restaurants International (“*YRI*”) from 2003 to 2005 and as its President from 1997 to 2003. Prior to that position, Mr. Bassi spent 25 years in a wide range of financial and general management positions at PepsiCo, Inc., Pepsi-Cola International, Pizza Hut (U.S. and International), Frito-Lay and Taco Bell. Mr. Bassi currently serves as lead director and Chair of the nominating and governance committee for each of BJ’s Restaurant and Potbelly Sandwich Works. He has been a member of each board of directors since 2004 and 2009, respectively. In addition, Mr. Bassi serves on the Value Optimization Board for the private equity firm Mekong Capital, based in Vietnam. Mr. Bassi served on the board of The Pep Boys—Manny, Moe & Jack from 2002 to 2009, and served on the board of Amrest Holdings (Poland) from 2012 to 2015. Mr. Bassi brings to our Board knowledge of the quick service restaurant industry and global franchising. In addition, he brings to our Board extensive public company board and corporate governance experience.



Ed Yiu-Cheong Chan

Age 54

Director Since 2016

Ed Yiu-Cheong Chan has served as Vice Chairman of Charoen Pokphand Group Company Limited and as an Executive Director and Vice Chairman of CP Lotus Corporation since 2012. Mr. Chan was Regional Director of North Asia of the Dairy Farm Group and a director of Dairy Farm Management Services Limited from November 2001 to November 2006. Mr. Chan was the President and Chief Executive Officer of Walmart China from November 2006 to October 2011. Mr. Chan is also a non-executive director of Treasury Wine Estates Limited, a company listed on the Australian Securities Exchange, and an independent non-executive director of Link Real Estate Investment Trust, which is listed on the Stock Exchange of Hong Kong Limited. Mr. Chan brings to our Board knowledge of the food and beverage industry in Asia and extensive public company board and corporate governance experience.



Edouard Ettegui

Age 65

Director Since 2016

Edouard Ettegui has served as the non-executive Chairman of Alliance Française, Hong Kong since 2016. He also serves as a non-executive director of Mandarin Oriental International Limited, the company for which he was the Group Chief Executive from 1998 to 2016. Prior to his time at Mandarin Oriental International, Mr. Ettegui was the Chief Financial Officer for Dairy Farm International Holdings, and he served in various roles for British American Tobacco, including Business Development Director, Group Finance Controller and Group Head of Finance. Mr. Ettegui has also held senior finance positions in seven countries at Philips International. Mr. Ettegui brings to our Board senior management experience in various international consumer-product industries, extensive financial expertise and public company board experience.

Continuing Class II Directors Whose Terms Will Expire in 2018



Louis T. Hsieh
Age 52
Director Since 2016

Louis T. Hsieh has served as a Senior Adviser to the Chief Executive Officer since 2016 and as a director since 2007 of New Oriental Education & Technology Group, a provider of private educational services in China. Prior to his current role, Mr. Hsieh served as that company's Chief Financial Officer from 2005 to 2015 and President from 2009 to 2016. In addition, Mr. Hsieh serves as an independent director, member of the corporate governance committee and chairman of the audit committee for JD.com, Inc, and independent director and Chairman of the audit committee for Nord Anglia Education, Inc. Previously, Mr. Hsieh also served as an independent director, member of the corporate governance committee and chairman of the audit committee for Perfect World Co., Ltd. and China Digital TV Holding Co., Ltd. Mr. Hsieh brings to our Board corporate leadership and public company board experience as well as his extensive financial and international business experience.



Jonathan S. Linen
Age 73
Director Since 2016

Jonathan S. Linen has been a member of the board of directors of Modern Bank, N.A. since 2005. Mr. Linen served as advisor to the Chairman of American Express Company, a financial services company, from January 2006 to July 2016. Prior to his role as advisor to the Chairman, Mr. Linen served as the Vice Chairman of American Express Company since August 1993. Mr. Linen served on the board of directors of YUM from 2005 to 2016 and of The Intercontinental Hotels Group from 2005 to 2015. In addition, Mr. Linen is a former director of Bausch & Lomb. Mr. Linen brings to our Board operating and management experience, expertise in finance, marketing and international business development and public company board and committee experience.



Micky Pant
Age 62
Director Since 2016

Micky Pant has served as the Chief Executive Officer of the Company since October 2016. He served as the Chief Executive Officer of the YUM China Division of YUM from August 2015 to October 2016. Since 2006, Mr. Pant has held a number of leadership positions at YUM, including the Chief Executive Officer of the KFC Division, CEO of YRI, President of Global Branding for YUM, President of YRI, Chief Marketing Officer of YUM, Global Chief Concept Officer for YUM and President of Taco Bell International. Before joining YUM, Mr. Pant built a foundation in marketing and international business with 15 years at Unilever in India and the U.K. and worked at PepsiCo, Inc. and Reebok International Limited. Since December 2014, Mr. Pant has served as an independent director on the board of Pinnacle Foods, Inc., where he also serves on the audit committee. Mr. Pant brings to our Board his vast knowledge of KFC and Pizza Hut best practices from around the globe and strategic, brand building expertise. In addition, Mr. Pant brings to our Board his corporate leadership knowledge and public company board experience.

Continuing Class III Directors Whose Term Will Expire in 2019



Christian L. Campbell

Age 66

Director Since 2016

Christian L. Campbell owns Christian L. Campbell Consulting LLC, which specializes in global corporate governance and compliance, and he has served as the owner of that entity since February 2016. Mr. Campbell previously served as Senior Vice President, General Counsel and Secretary of YUM from its formation in 1997 until his retirement in February 2016. In 2001, Mr. Campbell's role was expanded to include Chief Franchise Policy Officer. In these positions, Mr. Campbell oversaw all legal matters at YUM and was responsible for the oversight of YUM purchasing as a director of YUM's purchasing cooperative with its franchisees. Prior to joining YUM, Mr. Campbell was a Senior Vice President and General Counsel at Owens Corning, a leading global producer of fiberglass insulation and composite building materials. Prior to Owens Corning, he was Vice President and General Counsel for Nalco Chemical Company. In addition, Mr. Campbell was a founding director of Restaurant Supply Chain Solutions, Inc. ("*RSCS*"), a purchasing cooperative for YUM's U.S. franchising partners, and he served on RSCS's board of directors from its formation in 2001 until 2015. Mr. Campbell brings to our Board expertise in corporate governance and corporate compliance of publicly traded companies. In addition, Mr. Campbell brings to our Board extensive knowledge of the quick service restaurant industry, global franchising and corporate leadership.



Fred Hu

Age 53

Director Since 2016

Fred Hu is chairman and founder of Primavera Capital Group, a China-based global investment firm ("*Primavera*"). Dr. Hu has served as chairman of Primavera since its inception in 2010. Prior to Primavera, Dr. Hu served in various roles at Goldman Sachs from 1997 to 2010, including serving as chairman of Greater China at Goldman Sachs Group, Inc. From 1991 to 1996, Dr. Hu served as an economist at the International Monetary Fund (IMF) in Washington D.C., where he engaged in macroeconomic research, policy consultations and technical assistance for member country governments including China. Dr. Hu also served as director of the National Center for Economic Research and professor at Tsinghua University. He is the author of several books and other publications in the areas of economics and finance and on China and Asian economies. Dr. Hu has advised the Chinese government on financial and pension reform, state-owned enterprise (SOE) restructuring and macroeconomic policies. Dr. Hu is a trustee of China Medical Board and the co-chair of the Nature Conservatory's Asia Pacific Council. Dr. Hu brings to our Board extensive expertise in international affairs and the Chinese economy. In addition, Dr. Hu brings valuable business, strategic development and corporate leadership experience as well as expertise in economics, finance and global capital markets.



Ruby Lu
Age 46
Director Since 2016

Ruby Lu is an independent venture capitalist investing in technology start-ups in the U.S. and China. In 2006, she co-founded DCM China, an early-stage venture capital firm. During her more than 12-year tenure at DCM, she invested in and served as a board member for many leading technology companies including BitAuto Holdings Limited, E-Commerce China Dangdang Inc. and Pactera Technology International Ltd. She also served as an independent director and chairman of the special committee for iDreamSky Technologies Limited before it was taken private. She is currently an independent director and chairman of the special committee for iKang Healthcare Group, Inc. Prior to joining DCM in 2003, Ms. Lu was a vice president in the technology, media and telecommunications investment banking group of Goldman Sachs & Co. in Menlo Park, California. Ms. Lu brings to our Board public company board experience as well as extensive financial and global market experience.



Zili Shao
Age 57
Director Since 2016

Zili Shao has served as Partner at King & Wood Mallesons—China, a law firm, since April 2015. From 2009 to 2015, Mr. Shao held various positions with JPMorgan Chase & Co., a financial services company, including Chairman and Chief Executive Officer of JPMorgan China, Vice Chairman of JPMorgan Asia Pacific and Chairman of JPMorgan Chase Bank (China) Company Limited. Prior to JPMorgan, he was a partner with Linklaters LLP, a global law firm. He held positions as Greater China managing partner and managing partner of Asia Pacific. Mr. Shao brings to our Board extensive professional experience in Asia and public company board and corporate governance experience.

Item 2. Ratification of Independent Auditor

What am I voting on?

We are asking stockholders to approve a proposal to ratify the appointment of KPMG Huazhen LLP (“*KPMG*”) as our independent auditor for 2017. The Audit Committee has selected KPMG to audit our consolidated financial statements. During 2016, KPMG served as our independent auditor and also provided other audit-related and non-audit services.

Will a representative of KPMG be present at the Annual Meeting?

Representatives of KPMG will be present at the Annual Meeting, will have the opportunity to make a statement if they desire and will be available to respond to appropriate questions from stockholders.

What vote is required to approve this proposal?

Approval of this proposal requires the affirmative vote of a majority of the shares present in person or represented by proxy and entitled to vote at the Annual Meeting.

The Audit Committee and the Board of Directors recommend that you vote FOR approval of this proposal.

What were KPMG’s fees for audit and other services for 2016 and 2015?

The following table presents fees for professional services rendered by KPMG for the audit of the Company’s annual financial statements, and fees billed for audit-related services, tax services and all other services rendered by KPMG for 2016 and 2015. All KPMG services for 2016 and 2015 were approved in advance by the Audit Committee (or, prior to the spin-off, YUM’s audit committee) specifically or pursuant to procedures similar to those outlined below.

	2016	2015
Audit fees ⁽¹⁾	\$ 3,922,978	\$ 1,311,970
Audit-related fees ⁽²⁾	23,532	25,814
Tax fees ⁽³⁾	16,157	16,166
All other fees	—	—
TOTAL FEES	\$ 3,962,667	\$ 1,353,950

- (1) Audit fees include fees for the audit of the annual consolidated financial statements included in the Company’s annual reports, reviews of the interim condensed consolidated financial statements included in the Company’s quarterly reports, and services related to statutory filings or engagements. Audit fees in 2016 also includes fees for the audits of the combined financial statements of the Company for the three years ended December 31, 2015 and the interim review services rendered in connection with the Form 10 filed with the SEC and other services rendered in connection with the spin-off, which were paid by YUM.
- (2) Audit-related fees include audits of financial statements of certain employee benefit plans, agreed upon procedures and other attestations.
- (3) Tax fees consist principally of fees for tax filling assistance services.

What is the Company’s policy regarding the approval of audit and non-audit services?

The Audit Committee has implemented a policy for the pre-approval of all audit and permitted non-audit services, including tax services, proposed to be provided to the Company by its independent auditor. Under the policy, the Audit Committee may approve engagements on a case-by-case basis or pre-approve engagements on a categorical basis pursuant to the Audit Committee’s pre-approval policy. The Audit Committee may delegate pre-approval authority to one of its independent members and has currently delegated pre-approval authority up to certain amounts to its Chairperson.

In considering pre-approvals, the Audit Committee considers the nature, scope and fees of the service to be provided to the Company as well as the principles and guidance established by the SEC and the Public Company Accounting Oversight Board with respect to auditor independence. Services as to which a general pre-approval has been granted on an annual basis are effective for the applicable year. Any proposed service for which the estimated fees would cause the total fees for that class of service to exceed the applicable estimated fee threshold requires specific approval by the Audit Committee or its delegate.

The Principal Accounting Officer monitors the performance of all services provided by the independent auditor and determines whether such services are in compliance with this policy. The Principal Accounting Officer reports periodically to the Audit Committee with respect to compliance with this policy and the status of outstanding engagements, including actual services provided by the independent auditor and associated fees, and must promptly report to the Chairperson of the Audit Committee any non-compliance (or attempted non-compliance) with this policy of which the Corporate Controller becomes aware.

Item 3. Advisory Vote on Named Executive Officer Compensation

What am I voting on?

In accordance with SEC rules, we are asking stockholders to approve, on a non-binding basis, the compensation of the Company's named executive officers as disclosed in this proxy statement. This non-binding advisory vote is also known as the "Say on Pay" vote. This is not a vote on the Company's general compensation policies or the compensation of the Board.

Our performance-based executive compensation program is designed to attract, reward and retain the talented leaders necessary for our Company to succeed in the highly competitive market for talent, while maximizing stockholder returns. This approach has made our management team a key driver in the Company's strong performance over both the long and short term. We believe that our compensation program has attracted and retained strong leaders, and is closely aligned with the interests of our stockholders.

In deciding how to vote on this proposal, we urge you to read the Compensation Discussion and Analysis section of this proxy statement, beginning on page 27, which discusses in detail how our compensation policies and procedures operate and are designed to meet our compensation goals and how our Compensation Committee makes compensation decisions under our programs.

Accordingly, we ask our stockholders to vote in favor of the following resolution at the Annual Meeting:

"RESOLVED, that the compensation paid to the named executive officers, as disclosed in the Compensation Discussion and Analysis, the compensation tables and related materials included in the proxy statement, is hereby approved."

What vote is required to approve this proposal?

Approval of this proposal requires the affirmative vote of a majority of shares present in person or represented by proxy and entitled to vote at the Annual Meeting. While this vote is advisory and non-binding on the Company, the Board of Directors and the Compensation Committee will review the voting results and consider stockholder concerns in their continuing evaluation of the Company's compensation program.

What is the recommendation of the Board of Directors?

The Board of Directors recommends that you vote FOR approval of this proposal.

Item 4. Advisory Vote on the Frequency of the Advisory Vote on Named Executive Officer Compensation

What am I voting on?

In accordance with SEC rules, we are asking stockholders to determine, on a non-binding basis, whether the Say on Pay vote should occur every year, every two years or every three years. This non-binding advisory vote is also known as the “Say When on Pay” vote.

The Board has determined that holding the Say on Pay vote every year is the best approach for the Company because it provides more consistent and direct communication from our stockholders to the Board and the Compensation Committee regarding the compensation of our named executive officers.

Accordingly, the Board recommends that our stockholders vote in favor of the following resolution at the Annual Meeting:

“RESOLVED, that the option with the most votes cast shall be the desired frequency of the stockholders of the Company: (i) holding a non-binding advisory vote on the named executive officers’ compensation once every year; (ii) holding a non-binding advisory vote on the named executive officers’ compensation once every two years; or (iii) holding a non-binding advisory vote on the named executive officers’ compensation once every three years.”

What vote is required to approve this proposal?

Stockholders are not voting to approve or disapprove of the Board’s recommendation. Instead, stockholders may cast their vote in one of four manners with respect to this proposal: (1) one year; (2) two years; (3) three years; or (4) abstaining from voting on the proposal. The frequency with the most votes cast shall be the desired frequency of the stockholders of the Company. Although the vote is non-binding, we value continuing and constructive feedback from our stockholders on compensation and other important matters. The Board of Directors and the Compensation Committee will take into consideration the voting results when determining how often the Say on Pay vote should occur.

What is the recommendation of the Board of Directors?

The Board of Directors recommends that you vote FOR “every year” as the frequency which the non-binding advisory vote to approve named executive officer compensation should be held.

STOCK OWNERSHIP INFORMATION

Who are our largest stockholders?

The following table sets forth the number of shares of Company common stock beneficially owned as of February 28, 2017 by (i) beneficial owners of more than 5% of the outstanding shares of Company common stock, (ii) each of the Company's named executive officers, (iii) each of the Company's directors and director nominees and (iv) all of the Company's directors and executive officers as a group.

In accordance with SEC rules, beneficial ownership includes all shares the stockholder actually owns beneficially or of record, all shares over which the stockholder has or shares voting or dispositive control and all shares the stockholder has the right to acquire within 60 days of February 28, 2017. Except as indicated in the footnotes to the table, the Company believes that the persons named in the table have sole voting and investment power with respect to all shares owned beneficially by them.

Name of Beneficial Owner	Number of Shares Beneficially Owned	Percent of Shares ⁽¹⁾
<i>More than 5% owners</i>		
Primavera Capital Management Ltd. 28 Hennessy Road, 28 th Floor Hong Kong	30,982,892 ⁽²⁾	7.8%
Aberdeen Asset Management PLC 10 Queens Terrace Aberdeen, Scotland	23,906,833 ⁽³⁾	6.2%
BlackRock, Inc. 55 East 52 nd Street New York, NY 10055	21,674,803 ⁽⁴⁾	5.6%
<i>Named Executive Officers</i>		
Micky Pant	393,487 ⁽⁵⁾	*
Edwin "Ted" Stedem	32,546 ⁽⁶⁾	*
Joey Wat	10,641 ⁽⁷⁾	*
Christabel Lo	21,794 ⁽⁸⁾	*
Shella Ng	18,511 ⁽⁹⁾	*
<i>Non-Employee Directors</i>		
Peter A. Bassi	46,273	*
Christian L. Campbell	77,064 ⁽¹⁰⁾	*
Ed Yiu-Cheong Chan	8,339	*
Edouard Ettedgui	4,725	*
Louis T. Hsieh	9,080	*
Fred Hu	8,710	*
Jonathan S. Linen	54,107 ⁽¹¹⁾	*
Ruby Lu	8,339	*
Zili Shao	4,169	*
<i>Ownership of all directors and executive officers as a group (24 total)</i>	895,588⁽¹²⁾	*

* Represents less than one percent

(1) Percentage ownership is determined based on a total of 384,311,143 shares of Company common stock outstanding as of February 28, 2017.

(2) Based on Amendment No. 1 to the Schedule 13D filed by Primavera Capital Management Ltd. on January 19, 2017, which indicated that, as of January 9, 2017, Primavera Capital Management Ltd. had sole voting and

dispositive power over 30,982,892 shares of Company common stock, and Pollos Investment GP, Ltd. shared voting and dispositive control over 30,982,892 shares of Company common stock. Such amounts include 14,618,114 shares underlying outstanding warrants.

- (3) Based on the Schedule 13G filed by Aberdeen Asset Management PLC on February 8, 2017, which indicated that, as of December 30, 2016, Aberdeen Asset Management PLC had shared voting power over 17,749,636 shares of Company common stock and shared dispositive power over 23,906,833 shares of Company common stock.
- (4) Based on the Schedule 13G filed by BlackRock, Inc. on January 30, 2017, which indicated that, as of December 31, 2016, BlackRock, Inc. had sole voting power over 18,388,116 shares of Company common stock, shared voting power over 22,253 shares of Company common stock, sole dispositive power over 21,652,550 shares of Company common stock and shared dispositive power over 22,253 shares of Company common stock.
- (5) Includes 377,754 shares issuable upon the exercise of stock appreciation rights (“SARs”) that vest within 60 days of February 28, 2017.
- (6) Includes 26,618 shares issuable upon the exercise of SARs that vest within 60 days of February 28, 2017.
- (7) Reflects 5,954 shares issuable upon the exercise of SARs and 4,687 shares issuable upon the vesting of restricted stock units (“RSUs”), in each case that are exercisable or vest within 60 days of February 28, 2017.
- (8) Reflects 17,107 shares issuable upon the exercise of SARs and 4,687 shares issuable upon the vesting of RSUs, in each case that are exercisable or vest within 60 days of February 28, 2017.
- (9) Includes 12,324 shares issuable upon the exercise of SARs and 4,687 shares issuable upon the vesting of RSUs, in each case that are exercisable or vest within 60 days of February 28, 2017.
- (10) Includes 41,128 shares issuable upon the exercise of SARs that vest within 60 days of February 28, 2017. Also includes 80 shares held by Mr. Campbell’s spouse.
- (11) Includes 11,021 shares issuable upon the exercise of SARs that vest within 60 days of February 28, 2017. Also includes 15,864 shares held in a trust for which Mr. Linen is a trustee and 43 shares held by Mr. Linen’s spouse.
- (12) Includes 650,632 shares issuable upon the exercise of SARs and 44,516 shares issuable upon the vesting of RSUs, in each case that are exercisable or vest within 60 days of February 28, 2017.

SECTION 16(a) BENEFICIAL OWNERSHIP REPORTING COMPLIANCE

Section 16(a) of the Securities Exchange Act of 1934, as amended, requires our directors, executive officers and persons who own more than 10% of the outstanding shares of Company common stock to file with the SEC reports of their ownership and changes in their ownership of Company common stock. Directors, executive officers and greater-than-ten percent stockholders are also required to furnish to us copies of all ownership reports they file with the SEC. To our knowledge, based solely on a review of the copies of such reports and representations by our directors and executive officers that no other reports were required, all of the reports required to be filed by such persons during 2016 were timely filed.

EXECUTIVE COMPENSATION

COMPENSATION DISCUSSION AND ANALYSIS

Introduction

On October 31, 2016, the Company separated from Yum! Brands (“*YUM*”), becoming an independent publicly traded company as a result of a pro rata distribution to shareholders of YUM of one share of Company common stock for every one share of common stock held as of October 19, 2016 (the “*spin-off*”). This Compensation Discussion and Analysis describes the compensation received by the Company’s “named executive officers” in 2016 prior to and following the spin-off as well as certain compensation actions taken by the Compensation Committee of the Company’s Board (the “*Company Compensation Committee*”) following the spin-off. In view of the timing of the spin-off, most of the 2016 compensation decisions described in this Compensation Discussion and Analysis were determined by YUM rather than the newly formed Company Compensation Committee.

As a newly independent company, we expect the Company’s executive compensation program to evolve in support of its on-going business strategy. The Company Compensation Committee will review and consider modifications to the Company’s executive compensation program to reflect the Company’s business strategy, performance and evolving corporate governance practices.

Recently, the Company Compensation Committee has:

- Reviewed and approved the Company Compensation Committee Charter to ensure program and policy oversight and decision-making authority is held at what the committee considers to be the appropriate levels of the Board, Company Compensation Committee and management;
- Adopted a new approach to peer company selection that we believe better aligns with the executive selection and retention strategies of the Company and provides clearer comparability between the Company and the peer companies with regard to industry, geographic coverage and size;
- Reviewed the performance measures used in the annual incentive plan and revised financial performance ranges to better align the incentive payouts and the Company’s performance as an independent company while maintaining the existing executive compensation program and the focus on key performance measures of the Company’s overall business and operating segments for 2017; and
- Reviewed and approved the Compensation Recovery Policy, which may require an executive officer to return compensation paid or the Company to cancel performance awards previously granted to the executive officer, under certain circumstances as described in the policy.

During 2017, the Company Compensation Committee will review the executive compensation program including the annual and long-term incentive plans and the incentive vehicles used, the performance measures and other conditions used to determine the equity awards, as well as the share ownership guidelines for executives, in order to ensure alignment between pay and performance.

2016 Performance

2016 was a historic year for the Company, as we successfully completed our spin-off from YUM in October 2016 to become an independent company. By the end of 2016, the Company was the largest restaurant company in China with approximately 7,500 restaurants. Our restaurant base consists of KFC, the leading quick-service restaurant brand in China in terms of system sales and number of restaurants, Pizza Hut Casual Dining, the leading casual dining restaurant concept in China as measured by system sales and number of restaurants, Pizza Hut Home Service, Taco Bell, East Dawning and Little Sheep. Following the spin-off, we maintained the exclusive right to operate and sub-license the KFC, Pizza Hut and Taco Bell brands in China, and own the East Dawning and Little Sheep concepts outright.

Our 2016 performance highlights include the following:

- Total system sales for the year grew 5%, including growth of 6% at KFC and 3% at Pizza Hut Casual Dining, excluding foreign currency translation (“*F/X*”);
- We opened 575 new restaurants for the full year, or 5% net growth, surpassing 7,500 restaurants in China; and
- Reported operating profit for the year grew 31%.

Named Executive Officers

The Named Executive Officers (“*NEOs*”) for 2016 were as follows:

<u>Name</u>	<u>Title</u>
Micky Pant	Chief Executive Officer
Ted Stedem	Chief Financial Officer
Joey Wat ⁽¹⁾	President and Chief Operating Officer
Christabel Lo	Chief People Officer
Shella Ng	Chief Legal Officer and Corporate Secretary

(1) Effective February 8, 2017, Ms. Wat was appointed to the position of President and Chief Operating Officer of the Company. During 2016, Ms. Wat served as Chief Executive Officer, KFC China.

Compensation Philosophy

The Company’s historical executive compensation program has been designed to attract and retain the right talent to achieve superior stockholder results, support long-term growth of the Company while holding our executives accountable to achieve annual results year after year. In addition, the program has historically been designed to reward performance, emphasize long-term value creation and drive an ownership mentality.

The Company’s executive compensation program has three primary pay components: base salary, annual performance-based cash bonuses and long-term equity awards. These key elements are aligned with the Company’s compensation philosophy.

Objective	Base Salary	Annual Performance-Based Cash Bonuses	Long-Term Equity
Attract and retain the right talent to achieve superior stockholder results —Competitive total reward program structure that enables pay to vary based on role, responsibility, experience, market value and future potential of the talent in order to drive superior results year over year.	X	X	X
Reward performance —Motivate both short-term and long-term performance through annual and long-term equity programs. A significant portion of NEO pay is performance-based and therefore at-risk.		X	X
Emphasize long-term value creation —The Company’s belief is simple: if it creates long-term value for stockholders, then it shares a portion of that value with those responsible for the results. Stock Appreciation Rights (“ SARs ”) reward value creation generated from sustained results and the favorable expectations of the Company’s stockholders. Restricted Stock Units (“ RSUs ”) focus executives on the long-term performance of the Company and directly align the interests of executives with those of the Company’s stockholders.			X
Drive ownership mentality —The Company expects executives to personally invest in the Company’s success by owning a substantial amount of Company stock.			X

Overview of 2016 Compensation Decisions

Prior to the spin-off, the Company was part of YUM’s consolidated enterprise and our executive officers participated in the compensation programs of YUM. Many of the decisions affecting the Company’s executive compensation program were made in 2016 prior to the spin-off by the Management Planning & Development Committee of YUM’s Board (the “**YUM Compensation Committee**”) and some of those decisions were intended to facilitate the transition. Prior to the spin-off, the YUM Compensation Committee determined equity compensation with respect to all of our executive officers as well as the cash compensation with respect to Mr. Pant, our Chief Executive Officer. For other executive officers, their cash compensation was determined prior to the spin-off by the Chief Executive Officer of YUM (“**YUM CEO**”) and the China Division CEO, except that our CFO’s 2016 cash compensation before his appointment was determined by the YUM CEO and the KFC Division CEO. Following the spin-off, the executive compensation decisions have been reviewed by the Company Compensation Committee.

Key Compensation Decisions in Connection with the Spin-Off

In connection with the spin-off, the following key compensation decisions were made to facilitate the transition:

- *January 2016 Retention Grants* – In January 2016, YUM granted special retention awards in the form of RSUs to key executive talent in order to induce them to remain employed with the Company post-spin-off and to further align their interests with the Company’s stockholders post-spin-off. Under the terms of these awards, these RSUs were adjusted in the spin-off to represent equity awards with respect to the Company rather than an adjusted equity award with respect to both the Company and YUM. Mses. Wat, Lo and Ng each received these special retention awards.
- *Appointment of Mr. Stedem* – Effective August 1, 2016, Mr. Stedem was appointed to the position of Chief Financial Officer of YUM’s China Division. In connection with Mr. Stedem’s appointment, his base

salary and annual target opportunity were increased to reflect his anticipated role as CFO of an independent publicly traded company. Mr. Stedem's compensation adjustments were designed to retain Mr. Stedem post-spin-off and further incentivize his performance with the Company.

- *Appointment of Mr. Pant as CEO of the Company* – In October 2016, the Company entered into a letter of understanding with Mr. Pant outlining the compensation terms relating to his appointment to the position of Company CEO, including his post-spin-off base salary and annual target opportunity, his November 2016 Founders' Grants (as described below), the treatment of his YUM equity awards upon his separation from YUM, and his 2017 long-term incentive opportunity of \$4,000,000. Mr. Pant's compensation adjustments were designed to retain Mr. Pant post-spin-off and further incentivize his performance with the Company.
- *Adjustments to Outstanding Equity Awards* – Concurrent with the spin-off, holders of YUM equity-based awards, whether vested or unvested, generally received both adjusted YUM awards and Company awards, subject only to limited exceptions. Further, Mr. Pant, as a holder of Performance Share Units ("*PSUs*"), retained his outstanding PSUs as YUM awards, adjusted to reflect the effects of the spin-off. Generally, changes to outstanding employee awards made as a result of the spin-off were consistent with the changes made to the shareholdings of all YUM shareholders.
- *November 2016 Founders Grants* – In connection with the spin-off, the YUM Compensation Committee approved, and the Company Compensation Committee affirmed, grants of RSUs and SARs to the NEOs. These grants were intended to align the NEOs' interests with those of the Company, incentivize management to maximize the value of the Company and retain critical talent.

Key Compensation Decisions Following the Spin-Off

Following the spin-off, the Company Compensation Committee made the following compensation decisions to address the evolving nature of the Company as an independent publicly traded company. Key compensation decisions made following the spin-off include:

- *Development of Peer Group for 2017 Compensation Decisions* – The Company Compensation Committee retained Willis Towers Watson ("*WTW*") as its independent compensation consultant to advise on executive compensation matters. WTW's responsibilities for 2016 included advising the Company regarding the composition of the post-spin-off comparator peer group, providing input regarding post-spin-off compensation adjustments and the modification of the 2017 annual incentive program. WTW does not provide any other services to the Company.

With the assistance of its independent compensation consultant, the Company Compensation Committee adopted a new approach to peer company selection that we believe better aligns with the executive selection and retention strategies of the Company and provides clearer comparability between the Company and the peer companies with regard to industry, geographic coverage and size. For the purpose of evaluating 2017 compensation decisions, the Company developed two sets of peer companies for the NEOs and other executive officers. Recognizing that the Company's executive talents are sourced and recruited from a variety of industries and different geographical regions, the Company Compensation Committee has adopted (i) a Greater China peer group consisting of 18 publicly listed companies in the food and beverage ("*F&B*"), restaurant, retail, hospitality, consumer goods and general industries and of similar revenue size to the Company, and (ii) a U.S. peer group of 20 publicly listed companies in the restaurant, F&B, hospitality and consumer goods industries and of similar revenue size to the Company. The Company Compensation Committee believes that the use of these two peer groups is essential to reflect the broad spectrum and diversity of executive talent and pay practices in the two markets in which we compete for executive talent. Recognizing the evolving nature of the competitive landscape for executive talent, the Company Compensation Committee intends to reassess the peer companies on a periodic basis to evaluate the continued appropriateness of such peer companies.

- *Approved Compensation Committee Charter* – Following the spin-off, the Company Compensation Committee reviewed and approved the Company Compensation Committee Charter to ensure program

and policy oversight and decision-making authority is held at what the committee considers to be the appropriate levels of the Board, Company Compensation Committee and management.

- *Approved Compensation Recovery Policy* – To further align the Company’s compensation program with corporate governance best practices, the Company Compensation Committee reviewed and approved the Compensation Recovery Policy, which may require an executive officer to return certain compensation paid or the Company to cancel performance awards previously granted to the executive officer, under certain circumstances as described in the policy.
- *Review of Performance Measures* – In connection with setting 2017 compensation opportunities, the Company Compensation Committee reviewed the performance measures used in the annual incentive plan and revised financial performance ranges to better align the incentive payouts and the Company’s performance as an independent company while maintaining the existing executive compensation program and the focus on key performance measures of the Company’s overall business and business segments for 2017.

As a newly independent company, we expect the Company’s executive compensation program to evolve in support of our on-going business strategy. The Company Compensation Committee will review and consider modifications to the Company’s executive compensation program to reflect the Company’s business strategy, performance and evolving corporate governance practices.

Elements of the Executive Compensation Program

The executive compensation program has three primary pay components: base salary; annual performance-based cash bonuses; and long-term equity awards.

Base Salary. The Company provides a fixed level of cash compensation to attract and retain the right caliber talent. The base salary is in the form of cash to compensate its executives for their primary roles and responsibilities. An executive’s actual salary varies based on the role, level of responsibility, experience, individual performance, future potential and the market value of the role. After the spin-off, the Company’s Compensation Committee has taken over the responsibility to review the salary levels of the executive officers annually.

Annual Performance-Based Cash Bonuses. The principal purpose of this annual incentive program is to motivate and reward short-term team and individual performance. It is a cash-based plan. Prior to the spin-off in 2016, our executives participated in a performance-based annual bonus program as executives of YUM’s China Division. The performance goals were approved following the established process of YUM for its divisions at the beginning of 2016. The formula for calculating the 2016 performance-based annual bonus is the product of the following:

$$\begin{array}{ccccccc} \text{Base Salary} & \times & \text{Target Bonus} & \times & \text{Team Performance} & \times & \text{Individual Performance} & = & \text{Bonus Payout} \\ & & \text{Percentage} & & (0-200\%) & & (0-150\%) & & (0-300\%) \end{array}$$

As a result of the spin-off, the 2016 performance-based annual bonus program was bifurcated into two performance periods – pre-spin-off and post-spin-off performance periods. For the pre-spin-off performance period (from January 1, 2016 to October 31, 2016), executives had a portion of their bonuses tied to the performance of YUM, while the post-spin-off performance period (from November 1, 2016 to December 31, 2016) related solely to the performance of the Company and the participant’s area of responsibility.

In connection with setting 2017 compensation opportunities, the Company Compensation Committee reviewed the performance measures used in the annual incentive plan and revised financial performance ranges to better align the incentive payouts and the Company’s performance as an independent company, while maintaining the existing executive compensation program and the focus on key performance measures of the Company’s overall business and operating segments for 2017.

Team Performance. The YUM Compensation Committee established the performance measures, targets and weights in January 2016 after receiving input and recommendations from its management.

The performance objectives in 2016 were developed through YUM's and the Company's annual financial planning process, which took into account growth strategies, historical performance, and the expected future operating environment of each of YUM's Divisions, including the China Division. A leverage formula for each team performance measure magnifies the potential impact that performance above or below the performance target will have on the calculation of the annual bonus. This leverage increases the payouts when targets are exceeded and reduces payouts when performance is below target. There is a threshold level of performance for all measures that must be met in order for any bonus to be paid. Additionally, all measures have a cap on the level of performance above which no additional bonus will be paid regardless of performance above the cap.

The team performance targets, actual results, weights and overall performance for each measure for the Company's NEOs are outlined below.

COMPANY

<u>Team Performance Measures</u>	<u>Target</u>	<u>Actual</u>	<u>Earned As a% of Target</u>	<u>Weighting</u>	<u>Final Team Performance</u>
Adjusted Operating Profit Growth*	10%	25%	200	50%	100
Same Store Sales Growth	3%	0.40%	0	25%	0
System Gross New Builds	575	575	100	15%	15
System Customer Satisfaction	—	—	154	10%	15
FINAL COMPANY TEAM FACTOR	130				

COMPANY: KFC China

<u>Team Performance Measures</u>	<u>Target</u>	<u>Actual</u>	<u>Earned As a% of Target</u>	<u>Weighting</u>	<u>Final Team Performance</u>
Adjusted Operating Profit Growth*	9%	24%	200	50%	100
Adjusted Same Store Sales Growth**	4.60%	4.20%	82	25%	21
System Gross New Builds	270	323	200	15%	30
System Customer Satisfaction	88%	89.60%	162	10%	16
FINAL KFC China TEAM FACTOR	167				
YUM TEAM FACTOR***	163				
YUM: KFC Division TEAM FACTOR***	100				
YUM: KFC Asia TEAM FACTOR***	104				

* Adjusted Operating Profit Growth is the reported operating profit growth, excluding items that we believe are not directly relating to or impacted by the performance of the executives, such as the impact from retail tax structure reform and adjustments associated with the spin-off.

** Adjusted Same Store Sales Growth is the Same Stores Sales Growth disclosed in the Annual Report on Form 10-K, but adjusted for items to reflect how we evaluate same store sales growth for our brands internally.

*** Reflects performance factor, as calculated and disclosed to the Company by YUM.

NEO	Measures	Team Factor
Mr. Pant	Pre-Spin – weighted 75% Company + 25% YUM	138
	Post-Spin – weighted 100% Company	130
	FINAL TEAM FACTOR	137
Mr. Stedem	Singapore Period – weighted	103
	75% KFC Asia + 25% KFC Division	138
	Pre-Spin – weighted 75% Company + 25% YUM	130
	Post-Spin – weighted 100% Company	130
	FINAL TEAM FACTOR	119
Ms. Wat	Pre-Spin – weighted 75% KFC + 25% YUM	166
	Post-Spin – weighted 75% KFC + 25% Company	158
	FINAL TEAM FACTOR	165
Ms. Lo	Pre-Spin – weighted 75% Company + 25% YUM	138
	Post-Spin – weighted 100% Company	130
	FINAL TEAM FACTOR	137
Ms. Ng	Pre-Spin – weighted 75% Company + 25% YUM	138
	Post-Spin – weighted 100% Company	130
	FINAL TEAM FACTOR	137

Long-Term Equity Incentives. YUM has historically provided long-term equity compensation to its executives to encourage long-term decision making that creates sustainable stockholder value. In determining the size of the award, the YUM Compensation Committee considered the following:

- Prior year individual and team performance;
- Expected contribution in future years;
- Consideration of the market value of the executive’s role compared with similar roles in YUM’s historical peer group (or, in the case of the Company’s NEOs other than Mr. Pant, compensation survey data); and
- Achievement of YUM’s stock ownership guidelines.

Annual Equity Grants. For 2016, the YUM Compensation Committee granted SARs as the annual equity awards for each of our NEOs. These SARs have ten-year terms and vest over four years. The exercise price of each SAR grant was based on the closing market price of the underlying YUM common stock on the date of grant. Therefore, SAR awards will only have value if the share price appreciates above the awards’ exercise price.

Concurrently with the spin-off, holders of YUM equity-based awards (including SARs), whether vested or unvested, generally received both adjusted YUM awards and Company awards. Accordingly, each of our NEOs received both adjusted YUM awards and Company awards with respect to their outstanding SAR awards.

Spin-Off Grants. As noted above, in light of the spin-off, YUM approved special stock award grants for a number of Company executives and key employees, including the NEOs. These retention grants were intended to align the interests of participants with those of the Company, incentivize management to maximize the value of the Company, and retain critical talent. In January 2016, YUM granted special

equity incentive awards in the form of RSUs with respect to key executive talent in order to induce these executives to remain employed with the Company post-spin-off and to further align their interests with the Company's stockholders post-spin-off. Under the terms of these awards, these RSUs were adjusted in the spin-off to represent equity awards with respect to the Company rather than an adjusted equity award with respect to both the Company and YUM. Mses. Wat, Lo and Ng received these special awards, each with a grant date fair value equal to approximately \$400,000. These RSUs vest in 25% increments on the first and second anniversaries of the grant date, with the remaining 50% of the award vesting on the third anniversary of the grant date.

In connection with the spin-off, the YUM Compensation Committee approved, and the Company Compensation Committee affirmed, the award of Founder's Grants in November 2016. These Founder's Grants were delivered in the form of RSUs and SARs, with the following grant date values:

NEO	SARs ⁽¹⁾	RSUs ⁽²⁾
Mr. Pant	\$1,500,000	\$1,500,000
Mr. Stedem	\$ 500,000	\$ 500,000
Ms. Wat	\$ 500,000	\$ 500,000
Ms. Lo	\$ 250,000	\$ 250,000
Ms. Ng	\$ 250,000	\$ 250,000

(1) SARs Founders' Grants will vest 25% per year on each of the first four anniversaries of the grant date.

(2) RSU Founders' Grants will vest 50% on each of the second and third anniversaries of the grant date.

The Company also offers certain retirement and other benefits, including benefits relating to overseas service, that the Company believes are consistent with market practice for companies of a similar scope and nature attempting to recruit and retain high-performing, globally mobile executives.

2016 Named Executive Officer Total Direct Compensation and Performance Summary

Below is a summary of our NEOs' 2016 total direct compensation—which includes base salary, annual cash bonus, and the equity award delivered as SARs—and an overview of their 2016 performance relative to the annual performance goals. The special equity grants made in anticipation of, or in connection with, the spin-off are excluded from the following discussion as those grants do not represent an ongoing element of total direct compensation. As noted above, many of the compensation decisions described below were determined prior to the spin-off by YUM rather than the Company Compensation Committee. Following the spin-off in October 2016, executive compensation decisions have been, and will be, made by the Company Compensation Committee.

Micky Pant
Chief Executive Officer

2016 Performance Summary. Based on the recommendations of YUM's Board, the Company's Board determined Mr. Pant's performance to be significantly above target and awarded him a 140% individual performance factor. With a blended final team factor of 137%, Mr. Pant received 191% of his annual target bonus. In considering Mr. Pant's performance, YUM's Board and the Company's Board considered that Yum China, under the leadership of Mr. Pant, had achieved an adjusted operating profit growth of 25% while meeting the New Build target of 575 new restaurants. Mr. Pant was recognized for not only achieving strong operating and business results, but also his leadership in orchestrating the timely completion of the spin-off and the successful listing of the Company on the NYSE on November 1, 2016.

2016 Decisions. In November 2016, in order to recognize his past performance as well as his new and expanded responsibilities in running a public company, the YUM Compensation Committee adjusted Mr. Pant's compensation as follows:

- Base salary was \$1,100,000.
- Annual cash bonus target increased from 115% of base salary to 130% of base salary.

The table below summarizes how the annual performance-based incentive award was calculated for Mr. Pant:

2016 BONUS AWARD

Performance Period	Team Factor Weight	2016 Salary US\$	Target	Individual Performance Factor (IF)	Team Factor (TF)	Bonus US\$
Jan – Oct (Pre-Spin)	75% Company 25% YUM		115%		138%	
Nov – Dec (Post-Spin)	100% Company	1,100,000	130%	140%	130%	2,470,417

Ted Stedem
Chief Financial Officer

2016 Performance Summary. Mr. Stedem was the General Manager of KFC Asia prior to being appointed as the Chief Financial Officer of YUM's China Division on August 1, 2016. Mr. Stedem's performance was rated above target for his time in KFC Asia with YUM, and above target for his time with the Company. He was awarded an individual performance factor of 120%. With a blended team factor of 119%, Mr. Stedem received 143% of his annual target bonus. Mr. Stedem took over as CFO for the Company three months prior to the spin-off and was recognized for his leadership, rapidly taking charge, aligning the finance function, engaging and onboarding top talent to complete a number of complex projects including listing the Company on the NYSE, SEC reporting, and various tax matters. Mr. Stedem also played a key role in successfully implementing and maximizing benefits associated with a change in the tax structure in China.

2016 Decisions. In order to recognize his appointment as CFO of the Company, in August 2016, Mr. Stedem's compensation was adjusted by the YUM Compensation Committee as follows:

- Base salary was \$525,000.
- Annual cash bonus target increased from 45% of base salary to 65% of base salary.

The table below summarizes how the annual performance-based incentive award was calculated for Mr. Stedem:

2016 BONUS AWARD

Performance Period	Team Factor Weight	2016 Salary US\$	Target	Individual Performance Factor (IF)	Team Factor (TF)	Bonus US\$
Jan – July (Pre-Spin)	75% KFC Asia 25% KFC Division		45%		103%	
Aug – Oct (Pre-Spin)	75% Company 25% YUM	525,000	65%	120%	138%	400,712
Nov – Dec (Post-Spin)	100% Company				130%	

Joey Wat
 Chief Executive Officer, KFC China

2016 Performance Summary. Ms. Wat was the CEO of KFC China. Ms. Wat’s performance was rated significantly above target, and she was granted an individual performance factor of 140%. With a blended team factor of 165%, Ms. Wat received 230% of her annual target bonus. During 2016, Ms. Wat was in her third year leading the KFC brand and, during her tenure, led a comprehensive turnaround. In determining her payout, it was considered that, in 2016, the brand sales recovered and same store sales increased by 3%, KFC business achieved system sales growth of 6%, new builds of 323 restaurants as well as asset upgrades of an additional 720 stores during the year. Ms. Wat also formulated clear brand strategies and led the KFC team to improve on restaurant management team stability. KFC restaurant margins reached 16.3% and KFC operating profit was \$645 million, both ahead of target. Also, notable was the significant progress made in Digital and Delivery, with membership in KFC’s loyalty program surpassing 60 million.

2016 Decisions. In February 2016, Ms. Wat’s compensation was adjusted as follows:

- Base salary was \$628,300.
- Annual cash bonus target was 85% of base salary.

The table below summarizes how the annual performance-based incentive award was calculated for Ms. Wat:

2016 BONUS AWARD

Performance Period	Team Factor Weight	2016 Salary US\$	Target	Individual Performance Factor (IF)	Team Factor (TF)	Bonus US\$
Jan – Oct (Pre-Spin)	75% KFC 25% YUM				166%	
Nov – Dec (Post-Spin)	75% KFC 25% Company	628,300	85%	140%	158%	1,231,175

Compensation Adjustments in Connection with Promotion. As noted above, effective February 8, 2017, Ms. Wat was appointed to the position of President and Chief Operating Officer of the Company. In connection with Ms. Wat’s appointment, the Company Board approved an increase in Ms. Wat’s annual base salary from \$628,000 to \$750,000 and an increase in her annual performance-based cash bonus target from 85% to 100% of her annual base salary. The Board also approved a promotion grant of RSUs, with a grant date fair value of \$2,000,000. The RSUs cliff vest on the fourth anniversary of the date of grant, subject to Ms. Wat’s continued employment through the vesting date. Pursuant to the Company’s long-term incentive program, in 2017, Ms. Wat will also be eligible to receive SARs with a grant date face value of \$3,000,000. The SARs will have a ten-year term and vest in equal annual installments on each of the first four anniversaries of the date of grant, subject to Ms. Wat’s continued employment through the applicable vesting date.

Christabel Lo
Chief People Officer

2016 Performance Summary. During 2016, Ms. Lo served as the Chief People Officer and played a key support role as part of the project to separate Yum China into an independent company. Ms. Lo's performance was judged as significantly above target and she was awarded an individual performance factor of 140%. With a blended team factor of 137%, Ms. Lo received a bonus payout of 191% of her annual target bonus. Ms. Lo was recognized for her outstanding contributions to a number of strategic initiatives, including serving as a core member of the spin-off project, bringing in top talent across functions to support the successful listing of the Company, formulating and cascading a new Company vision and culture across the organization, and establishing the Centralized Shared Services Center which delivered significant productivity gains for the Company's human resources operations. Ms. Lo's 20 years of experience with the Company and her deep knowledge of the Company were considered critical to the successful separation of the Company into an independent company.

2016 Decisions. In February 2016, Ms. Lo's compensation was adjusted as follows:

- Base salary was \$340,000.
- Annual cash bonus target was 60% of base salary.

In July 2016, in recognition of Ms. Lo's expanded role and responsibilities and work schedule, her base salary was increased to \$400,000.

The table below summarizes how the annual performance-based incentive award was calculated for Ms. Lo:

2016 BONUS AWARD						
Performance Period	Team Factor Weight	2016 Salary US\$	Target	Individual Performance Factor (IF)	Team Factor (TF)	Bonus US\$
Jan – Oct (Pre-Spin)	75% Company 25% YUM				138%	
Nov – Dec (Post-Spin)	100% Company	400,000	60%	140%	130%	459,200

Shella Ng
Chief Legal Officer and Corporate Secretary

2016 Performance Summary. During 2016, Ms. Ng served as the Chief Legal Officer. Ms. Ng's performance was significantly above target and she was awarded an individual performance factor of 140%. With a blended team factor of 137%, Ms. Ng received 191% of her annual target bonus. Ms. Ng was noted for her superb contributions to the completion of the spin-off. In addition, in determining her bonus payout, she was recognized for her leadership role in the successful negotiation with YUM on intellectual property, tax, royalty terms and several other complex matters connected with the spin-off. Ms. Ng also completed all related legal documentation and filings pursuant to regulatory requirements while successfully discharging her ongoing role as Chief Legal Officer. Ms. Ng also has over 20 years of experience with the Company and her know-how was considered critical to providing a strong legal and corporate foundation to the new company.

2016 Decisions. In February, Ms. Ng's compensation was adjusted as follows:

- Base salary was \$370,307.
- Annual cash bonus target was 60% of base salary.

The table below summarizes how the annual performance-based incentive award was calculated for Ms. Ng:

2016 BONUS AWARD

Performance Period	Team Factor Weight	2016 Salary US\$	Target	Individual Performance Factor (IF)	Team Factor (TF)	Bonus US\$
Jan – Oct (Pre-Spin)	75% Company 25% YUM				138%	
Nov – Dec (Post-Spin)	100% Company	370,307	60%	140%	130%	425,112

Retirement and Other Benefits

As with all Company employees, Company executive officers receive certain employment and post-employment benefits. Benefits are an important part of retention and capital preservation for all levels of employees. Our benefits are designed to protect against the expense of unexpected catastrophic loss of health and/or earnings potential, and provide a means to save and accumulate for retirement or other post-employment needs.

Retirement Plans. For executives who were hired or re-hired after September 30, 2001, YUM has implemented the Leadership Retirement Plan (“*YUMLRP*”). This is an unfunded, unsecured account-based retirement plan which allocates a percentage of pay to an account payable to the executive following the later to occur of the executive’s separation of employment or attainment of age 55. In connection with the spin-off, the Company adopted the Yum China Holdings, Inc. Leadership Retirement Plan (“*YCHLRP*”), the terms of which are substantially similar to the terms of the YUMLRP. For 2016, Messrs. Pant and Stedem were eligible for and received annual allocations to their accounts equal to 20% and 8%, respectively, of base salary and target bonus.

The Company offers certain executives working in China retirement benefits under the Bai Sheng Restaurants (Hong Kong) Limited Retirement Scheme. The scheme was registered as Yum! Restaurants (Hong Kong) Limited Retirement Scheme prior to the spin-off. Under this program, the Company provides a company-funded contribution ranging from 5% to 10% of an executive’s base salary. During 2016, Ms. Wat, Ms. Lo and Ms. Ng were participants in the program. The Company’s contribution for 2016 was equal to 5%, 10% and 10% of salary for Ms. Wat, Ms. Lo and Ms. Ng, respectively. Upon termination, participants will receive a lump sum equal to a percentage of the Company’s contributions inclusive of investment return. This percentage is based on a vesting schedule that provides participants with a vested 30% interest upon completion of a minimum of three years of service, and an additional 10% vested interest for each additional completed year, up to a maximum of 100%.

In addition, prior to the spin-off, Messrs. Pant and Stedem participated in the Executive Income Deferral (“*EID*”) Program, an unfunded, deferred compensation plan maintained by YUM. The Company did not adopt the EID post spin-off or assume any account balances or liabilities with respect to the EID following the spin-off.

Medical, Dental, Life Insurance and Disability Coverage. The Company also provides other benefits such as medical, dental, life insurance and disability coverage to its executive officers through benefit plans, which are also provided to all eligible China-based employees. Prior to the spin-off, Mr. Pant and Mr. Stedem were eligible to purchase additional life, dependent life and accidental death and dismemberment coverage as part of their employee benefits package.

Perquisites. Certain perquisites are provided to certain Company executive officers relating to overseas assignments. These perquisites are governed by the Company’s formal mobility policy and are offered on a case-by-case basis reflecting each executive’s particular circumstances but generally reflect market practices for similarly situated, globally mobile executives working in international companies based in Mainland China. For example, our NEOs receive tax equalization benefits relating to their overseas assignments. These tax equalization payments as well as the other overseas assignment allowances provided are intended to ensure that our executives serving on overseas assignments are in the same approximate financial position as they would have been if they

have remained in their home countries during their time on overseas assignment. In addition, pursuant to Mr. Pant's letter of understanding with the Company, he is eligible to receive transportation and housing reimbursement and tax equalization payments while he is performing services in China. These perquisites are intended to help the Company attract and retain high-performing executives from different countries who have the skill sets and experiences to successfully manage and lead the Company while living in Mainland China. These perquisites may include housing reimbursement, mobility allowances, home leave expenses, cost of living allowances, tax preparation services and tax reimbursements for such perquisites and allowances. See the 2016 All Other Compensation Table for details.

How Compensation Decisions Are Made

Role of the Compensation Committee. Prior to the spin-off, the YUM Compensation Committee determined equity compensation with respect to our executive officers as well as the cash compensation with respect to Mr. Pant, our CEO. For other executive officers, except Mr. Stedem prior to his appointment to the CFO role, their cash compensation was determined prior to the spin-off by the YUM CEO and Mr. Pant. Following the spin-off, executive compensation decisions have been, and will be, made by the Company Compensation Committee. Prior to his appointment as CFO of the Company, Mr. Stedem's cash compensation was determined by the YUM CEO and the KFC Division CEO.

Role of the Independent Consultant. Prior to the spin-off, the YUM Compensation Committee retained Meridian Compensation Partners, LLC ("*Meridian*") as its independent compensation consultant. Following the spin-off, the Company Compensation Committee retained WTW to advise on executive compensation matters. WTW's responsibilities for 2016 included advising the Company regarding the composition of the post-spin-off comparator peer group, providing input regarding post-spin-off compensation adjustments and the modification of the 2017 annual incentive program. WTW does not provide any other services to the Company. The Company Compensation Committee has assessed the independence of WTW pursuant to the NYSE rules and the Company has concluded that WTW's work for the Company Compensation Committee does not raise any conflicts of interest.

Competitive Market Review.

Pre-Spin-Off Competitive Market Review

Compensation awarded prior to the spin-off was subject to a competitive market review process followed by the YUM Compensation Committee. For Mr. Pant, the YUM Compensation Committee compared his compensation to similarly situated executives at companies that comprised its executive peer group (the "*YUM Peer Group*"). For our other executive officers, their compensation was evaluated based on compensation survey data from multiple third-party providers, including Mercer, WTW and Aon Hewitt.

The 2016 YUM Peer Group consisted of the following companies:

AutoZone Inc.	Hilton Worldwide Holdings Inc.	Marriott International
Avon Products Inc.	Kellogg Company	Nike Inc.
Campbell Soup Company	Kimberly-Clark Corporation	Staples Inc.
Colgate Palmolive Company	Kohl's Corporation.	Starbucks Corporation
Gap Inc.	Macy's Inc.	Starwood Hotels & Resorts
General Mills Inc.	McDonald's Corporation	Worldwide, Inc.

Post-Spin-Off 2017 Competitive Market Review

As noted above, one of the key objectives of our executive compensation program is to retain and reward the right talent by providing competitive compensation. Given the change in business size, structure and focus of the Company as compared to YUM following the spin-off, the Company Compensation Committee determined that it should establish a new peer group applicable to the Company on a go-forward basis. As part of its engagement with the Company Compensation Committee, WTW assisted with the development of the post-spin-off peer group.

Recognizing the evolving nature of the competitive landscape for executive talent, however, the Company Compensation Committee intends to reassess the peer companies on a periodic basis to evaluate the continued appropriateness of such peer companies.

Based on its review and considering the skills, background and understanding of the business and regulatory environments that are required of the management team to run a U.S. listed and registered company with all operations in China, WTW developed two sets of peer companies with the following characteristics:

- Publicly listed Greater China companies primarily in the F&B, restaurant, retail, hospitality, and consumer goods and general industry and of similar revenue size to the Company.
 - For Greater China companies, additional criteria are applied to include companies of similar market prominence and having a globally mobile executive team and appropriate pay governance practices and processes in place.
- Publicly listed U.S. companies in the restaurant, F&B, hospitality and consumer goods industry and of similar revenue size as the Company.

Having considered the peer group selection criteria above and the comparability of each of the peer companies in terms of business size, industry, regulatory environment and source of executive talent, the Company Compensation Committee approved the following two peer groups of companies to be used for purposes of evaluating 2017 executive compensation decisions:

Greater China Peer Group

Cathay Pacific Airways Limited
 China Mengniu Dairy Co. Ltd.
 Chow Tai Fook Jewellery Group Ltd.
 CLP Holdings Ltd.
 Dah Chong Hong Holdings Limited
 Esprit Holdings Limited
 Inner Mongolia Yili Industrial Group Co., Ltd
 MGM China Holdings Limited
 Sands China Ltd.
 Shangri-La Asia Limited
 SJM Holdings Limited
 Swire Pacific Limited
 Swire Properties Limited
 Techtronic Industries Company Limited
 Want Want China Holdings Ltd.
 WH Group Limited
 Wilmar International Limited
 Wynn Macau Ltd.

U.S. Peer Group

AutoZone, Inc.
 Bloomin' Brands, Inc.
 Brinker International, Inc.
 Colgate-Palmolive Company
 Constellation Brands, Inc.
 Darden Restaurants, Inc.
 Domino's Pizza, Inc.
 Dr Pepper Snapple Group, Inc.
 General Mills, Inc.
 Hilton Worldwide Holdings Inc.
 Hyatt Hotels Corporation
 Kimberly-Clark Corporation
 Marriott International, Inc.
 McDonald's Corporation
 Molson Coors Brewing Company
 The Coca-Cola Company
 The Hershey Company
 The Wendy's Company
 Wyndham Worldwide Corporation
 Yum Brands, Inc.

The Company's revenue size falls at or about the median of each of the peer groups.

Compensation Policies and Practices

Payments upon Termination of Employment. The Company currently does not have agreements with its executives concerning severance payments upon termination of employment or a change in control of the Company. With the assistance of WTW, the Company Compensation Committee anticipates reviewing market practices with respect to severance arrangements and may in the future enter into severance and/or change in control agreements with the

Company's executive officers. The award agreements with respect to the Company's outstanding equity awards provide for "double trigger" vesting pursuant to which outstanding awards will fully and immediately vest only if the executive is employed on the date of a change in control of the Company and is involuntarily terminated (other than for cause) on or within two years following the change in control. In addition, in the case of an executive officer's retirement, the Company provides retirement benefits described above, life insurance benefits and the continued ability to exercise vested SARs/Options in accordance with the underlying award agreements.

Compensation Recovery Policy. Following the spin-off, the Company Compensation Committee adopted the Compensation Recovery Policy. Pursuant to the policy, in the event of any restatement of the Company's financial statements due to material noncompliance with any financial reporting requirement under the securities laws, the Company Compensation Committee shall recover or cancel any performance awards which were awarded to a current or former executive officer as a result of achieving performance targets that could not have been met under the restated results. The Company's recovery authority applies to any performance award received by such individual during the three completed fiscal years immediately preceding the date on which the Company is required to prepare the restatement. Under the terms of the policy, a performance award means any cash or equity-based award that is made, vests or is payable based wholly or in part on the results of a financial reporting measure.

Hedging and Pledging of Company Stock. Under the Company's Code of Conduct, no employee or director is permitted to engage in securities transactions that would allow them either to insulate themselves from, or profit from, a decline in the Company's stock price. Similarly, no employee or director may enter into hedging transactions in Company stock. Such transactions include (without limitation) short sales as well as any hedging transactions in derivative securities (*e.g.*, puts, calls, swaps, or collars) or other speculative transactions related to the Company's stock. Pledging of Company stock by executive officers and directors is also prohibited.

COMPENSATION COMMITTEE REPORT

The Compensation Committee has reviewed and discussed the Compensation Discussion and Analysis with management.

Based on such review and discussion with management, the Compensation Committee recommended to the Board of Directors that the Compensation Discussion and Analysis be included in this proxy statement and incorporated by reference in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2016.

Compensation Committee:
Edouard Ettegui (Chair)
Jonathan S. Linen

2016 SUMMARY COMPENSATION TABLE

The following table and footnotes summarize the total compensation awarded to, earned by or paid to the NEOs for fiscal year 2016 and, to the extent required by SEC executive compensation disclosure rules, fiscal years 2015 and 2014. The Company's NEOs are its Chief Executive Officer, Chief Financial Officer, and the three other most highly compensated executive officers for the 2016 fiscal year.

Name and Principal Position	Year	Salary(\$) ⁽¹⁾	Bonus(\$)	Stock Awards(\$) ⁽²⁾	Option/SAR Awards(\$) ⁽³⁾	Non-Equity Incentive Plan Compensation(\$) ⁽⁴⁾	Change in Pension Value and Nonqualified Deferred Compensation Earnings(\$) ⁽⁵⁾	All Other Compensation(\$) ⁽⁶⁾	Total(\$) ⁽⁷⁾
(a)	(b)	(c)	(d)	(e)	(f)	(g)	(h)	(i)	
Micky Pant Chief Executive Officer	2016	1,013,645	—	1,500,007	4,500,017	2,470,417	63,974	881,776	10,429,836
	2015	849,038	—	355,012	1,419,011	1,473,548	42,979	950,622	5,090,210
	2014	750,000	—	350,019	1,475,973	799,500	32,735	313,356	3,721,583
Ted Stedem Chief Financial Officer	2016	439,931	—	500,020	649,072	400,712	229	829,754	2,819,718
	2015	356,280	—	—	120,076	160,867	—	514,250	1,151,473
Joey Wat Chief Executive Officer, KFC China	2016	626,775	—	899,486	1,096,251	1,231,175	—	979,262	4,832,949
	2015	590,000	—	—	1,059,813	518,500	—	1,560,728	3,729,041
Christabel Lo Chief People Officer	2016	368,425	—	649,489	498,436	459,200	—	1,882,335	3,857,885
Shella Ng Chief Legal Officer and Corporate Secretary	2016	369,408	—	649,489	418,935	425,112	—	854,506	2,717,450
	2015	359,243	—	—	185,558	135,147	—	900,935	1,580,883

- (1) Amounts shown are not reduced to reflect the NEOs' elections, if any, to defer receipt of salary into the EID Program, a legacy plan sponsored by YUM.
- (2) The amounts reported in this column for 2016 represent the grant date fair value of the January RSU awards granted to Ms. Wat, Ms. Lo and Ms. Ng and the November RSU awards granted to each of the Named Executive Officers in connection with the spin-off, calculated in accordance with Accounting Standards Codification Topic 718 ("ASC 718"), Compensation-Stock Compensation. See Note 15 to the Company's Consolidated and Combined Financial Statements included in the Annual Report on Form 10-K for the year ended December 31, 2016 (the "Audited Financial Statements").
- (3) The amounts reported in this column for 2016 represent the grant date fair value of the annual SAR awards and the SAR awards granted to each of the Named Executive Officers in connection with the spin-off, calculated in accordance with ASC 718. See Note 15 to the Company's Audited Financial Statements for a discussion of the relevant assumptions used in calculating these amounts.
- (4) Amounts in this column reflect the annual incentive awards earned for the applicable fiscal year performance periods under the annual bonus program, which is described further in our Compensation Discussion and Analysis under the heading "Annual Performance-Based Cash Bonuses."
- (5) Pursuant to SEC disclosure rules, the amounts reported for Messrs. Pant and Stedem represent above market earnings credited under the YCHLRP that exceeds 120% of the applicable federal long-term rate. Please see the narrative accompanying the "2016 Nonqualified Deferred Compensation" table for further information regarding the YCHLRP.
- (6) The amounts in this column for 2016 are explained in the All Other Compensation Table and footnotes to that table, which follows.
- (7) Certain compensation included in the All Other Compensation column was denominated in Chinese Renminbi. Ms. Ng's salary and 2016 bonus award were denominated in Hong Kong dollars and these figures were converted to U.S. dollars using an exchange rate of 6.8346 and 7.7580, respectively, for disclosure purposes.

2016 ALL OTHER COMPENSATION TABLE

The following table and footnotes summarize the compensation and benefits included under All Other Compensation in the 2016 Summary Compensation Table that were awarded to, earned by or paid to the Company's NEOs, for the fiscal year ending December 31, 2016.

Name	Perquisites and other personal benefits (\$) ⁽¹⁾	Tax Reimbursements (\$) ⁽²⁾	Insurance premiums (\$) ⁽³⁾	Retirement Scheme Contributions (\$) ⁽⁴⁾	Other (\$) ⁽⁵⁾	Total (\$)
(a)	(b)	(c)	(d)	(e)	(f)	(g)
Mr. Pant	118,230	258,274	16,595	456,608	32,069	881,776
Mr. Stedem	283,247	240,208	316	79,366	226,617	829,754
Ms. Wat	136,675	652,193	—	31,356	159,038	979,262
Ms. Lo	153,496	1,643,506	—	36,861	48,472	1,882,335
Ms. Ng	93,012	685,003	—	36,941	39,550	854,506

- (1) Amounts in this column represent: for Mr. Pant, a housing reimbursement; for Mr. Stedem, an education reimbursement (\$157,953) and housing reimbursement (\$125,295); for Ms. Wat, an education reimbursement (\$14,134) and housing reimbursement (\$122,541); for Ms. Lo, an education reimbursement (\$36,613) and housing reimbursement (\$116,883); and for Ms. Ng, a housing reimbursement. Such amounts are valued based on the amounts paid directly to these NEOs or the service provider, as applicable.
- (2) Amounts in this column represent tax reimbursements for salary and the expenditure/housing allowances. These tax reimbursements as well as the other overseas assignment allowances provided are intended to ensure that our executives serving on overseas assignments are in the same approximate financial position as they would have been if they have remained in their home country during their time on overseas assignment.
- (3) These amounts reflect the income each NEO was deemed to receive from IRS tables related to YUM-provided life insurance in excess of \$50,000.
- (4) This column represents allocations to the YUMLRP and the YCHLRP for Messrs. Pant and Stedem and contributions to the Bai Sheng Restaurants (Hong Kong) Limited Retirement Scheme for Mses. Wat, Lo and Ng.
- (5) This column reports the total amount of other benefits provided. Other than for certain benefits of Mr. Stedem and Ms. Wat described below, none of the other benefits individually exceeded the greater of \$25,000 or 10% of the total amount of these other benefits and the perquisites and other personal benefits shown in column (b) for the NEO. These other benefits include mobility premiums, temporary living expenses, relocation expenses, home leave expenses, transportation expenses, and annual leave payouts. For 2016, Mr. Stedem and Ms. Wat received mobility premiums of \$63,028 and \$102,149, respectively, and Mr. Stedem received a temporary living / lodging of \$72,689 each of which exceeds 10% of the total amount of other benefits and the perquisites and other personal benefits that Mr. Stedem and Ms. Wat received. These amounts were valued based on the amounts paid directly to the NEO or the service provider, as applicable.

2016 GRANTS OF PLAN-BASED AWARDS

The following table provides information on the annual incentive program that the Company's NEOs participated in during 2016 and the SARs and RSUs granted in 2016 to the Company's NEOs. The table below includes equity granted prior to the spin-off by YUM. These shares were granted by YUM and were converted using the volume weighted average per share price of one share of the Company, trading "regular-way," as reported on the NYSE on the first post-distribution trading day. In addition to receiving a proportional number of Company shares during the conversion, the NEOs also received shares of YUM with respect to the pre-spin-off awards other than the January 4, 2016 grants to Mses. Wat, Lo and Ng. The YUM shares received upon conversion of the NEO's outstanding equity awards are excluded from this table. Awards made after the spin-off were determined based on the Company's stock price on the date of such grant.

Name	Issuer	Grant Date	Estimated Possible Payouts Under Non-Equity Incentive Plan Awards ⁽¹⁾			Estimated Future Payouts Under Equity Incentive Plan Awards			All Other Stock Awards; Number of Shares of Stock or Units ⁽²⁾	All Other Option/SAR Awards; Number of Securities Underlying Options ⁽³⁾	Exercise or Base Price Option/SAR Awards ⁽⁴⁾	Grant Date Fair Value ⁽⁵⁾
			Threshold (\$)	Target (\$)	Maximum (\$)	Threshold (#)	Target (#)	Maximum (#)				
(a)		(b)	(c)	(d)	(e)	(f)	(g)	(h)	(i)	(j)	(k)	(l)
Mr. Pant	—	—	—	1,292,500	3,877,500	—	—	—	—	—	—	—
	YUM	2/5/2016	—	—	—	—	—	—	—	210,527	69.76	3,000,010
	YUMC	11/11/2016	—	—	—	—	—	—	55,597	—	—	1,500,007
Mr. Stedem	YUMC	11/11/2016	—	—	—	—	—	—	—	146,538	26.98	1,500,007
	—	—	—	280,143	840,429	—	—	—	—	—	—	—
	YUM	2/5/2016	—	—	—	—	—	—	—	10,461	69.76	149,069
Ms. Wat	YUMC	11/11/2016	—	—	—	—	—	—	18,533	—	—	500,020
	YUMC	11/11/2016	—	—	—	—	—	—	—	48,846	26.98	500,002
	—	—	—	534,055	1,602,165	—	—	—	—	—	—	—
Ms. Lo	YUM	1/4/2016	—	—	—	—	—	—	5,532	—	—	399,466
	YUM	2/5/2016	—	—	—	—	—	—	—	41,842	69.76	596,249
	YUMC	11/11/2016	—	—	—	—	—	—	18,533	—	—	500,020
	YUMC	11/11/2016	—	—	—	—	—	—	—	48,846	26.98	500,002
Ms. Ng	—	—	—	240,000	720,000	—	—	—	—	—	—	—
	YUM	1/4/2016	—	—	—	—	—	—	5,532	—	—	399,466
	YUM	2/5/2016	—	—	—	—	—	—	—	17,434	69.76	248,435
	YUMC	11/11/2016	—	—	—	—	—	—	9,267	—	—	250,024
	YUMC	11/11/2016	—	—	—	—	—	—	—	24,423	26.98	250,001
Ms. Ng	—	—	—	222,184	666,552	—	—	—	—	—	—	—
	YUM	1/4/2016	—	—	—	—	—	—	5,532	—	—	399,466
	YUM	2/5/2016	—	—	—	—	—	—	—	11,855	69.76	168,934
	YUMC	11/11/2016	—	—	—	—	—	—	9,267	—	—	250,024
	YUMC	11/11/2016	—	—	—	—	—	—	—	24,423	26.98	250,001

- (1) Amounts in columns (c), (d) and (e) provide the minimum amount, target amount and maximum amount payable as annual incentive compensation under the 2016 annual bonus program based on respective team performances and on individual performance during 2016. The actual amount of annual incentive compensation awards paid for 2016 performance are shown in column (g) of the 2016 Summary Compensation Table. The performance measurements, performance targets, and target bonus percentages are described in the Compensation Discussion and Analysis beginning under the discussion of annual incentive compensation.
- (2) RSUs allow the grantee to receive the number of shares of the underlying common stock subject to the award upon vesting. The RSUs granted on January 4, 2016 vest 25% on each of the first and second anniversaries of the grant date and the remaining 50% vests on the third anniversary of the grant date, subject to the recipient's continued employment. The RSUs granted on November 11, 2016 vest 50% on each of the second and third anniversaries of the grant date, subject to the recipient's continued employment.
- (3) SARs allow the grantee to receive, in cash or the number of shares of the underlying common stock that, in each case, is equal in value to the appreciation in the underlying common stock with respect to the number of SARs granted from the date of grant to the date of exercise. SARs become exercisable in equal installments on the first, second, third and fourth anniversaries of the grant date, subject to the recipient's continued employment.
- (4) The exercise price of the SARs equals the closing price of the underlying common stock on the respective grant dates.
- (5) The amounts reported in this column for 2016 represent the grant date fair value of the annual SAR awards and the SAR and RSU awards granted to each of the NEOs in connection with the spin-off, calculated in accordance with ASC 718. See Note 15 to the Company's Audited Financial Statements for a discussion of the relevant assumptions used in calculating these amounts.

OUTSTANDING EQUITY AWARDS AT 2016 YEAR-END

The following table shows the number of Company shares covered by exercisable and unexercisable SARs, and RSUs held by the Company's NEOs on December 31, 2016. This table excludes the equity awards of YUM that were received in connection with the spin-off as those equity awards represent awards of YUM rather than of the Company and will be administered by YUM following the spin-off. Please see the Compensation Discussion and Analysis for a discussion of the adjustment to equity awards in connection with the spin-off.

Name	Grant Date	Option/SAR Awards				Stock Awards			
		Number of Securities Underlying Unexercised Options/SARs (#) Exercisable	Number of Securities Underlying Unexercised Options/SARs (#) Unexercisable ⁽¹⁾	Option/SAR Exercise Price (\$)	Option/SAR Expiration Date	Number of Shares or Units of Stock That Have Not Vested (#) ⁽²⁾	Market Value of Shares or Units of Stock That Have Not Vested (\$) ⁽³⁾	Equity incentive plan awards: Number of unearned shares, units or other rights that have not vested (#)	Equity incentive plan awards: market or payout value of unearned shares, units or other rights that have not vested (\$)
(a)	(b)	(c)	(d)	(e)	(f)	(g)	(h)	(i)	(j)
Mr. Pant	1/24/2008	52,833	—	11.26	1/24/2018	—	—	—	—
	1/24/2008	34,707	—	11.26	1/24/2018	—	—	—	—
	2/5/2009	133,503	—	8.84	2/5/2019	—	—	—	—
	2/5/2010	113,250	—	9.96	2/5/2020	—	—	—	—
	2/4/2011	100,468	—	14.88	2/4/2021	—	—	—	—
	11/18/2011	93,672	—	16.25	11/18/2021	—	—	—	—
	2/8/2012	114,478	—	19.46	2/8/2022	—	—	—	—
	2/6/2013	67,334	22,445 ⁽ⁱ⁾	19.00	2/6/2023	—	—	—	—
	2/5/2014	41,802	41,803 ⁽ⁱⁱ⁾	21.30	2/5/2024	—	—	—	—
	2/6/2015	21,990	65,970 ⁽ⁱⁱⁱ⁾	22.32	2/6/2025	—	—	—	—
	2/5/2016	—	207,883 ^(iv)	21.06	2/5/2026	—	—	—	—
	11/11/2016	—	146,538 ^(v)	26.98	11/11/2026	55,597 ⁽ⁱ⁾	1,452,194	—	—
	Mr. Stedem	2/4/2011	23,618	—	14.88	2/4/2021	—	—	—
2/4/2011		14,507	—	14.88	2/4/2021	—	—	—	—
2/8/2012		13,730	—	19.46	2/8/2022	—	—	—	—
2/6/2013		9,422	3,141 ⁽ⁱ⁾	19.00	2/6/2023	—	—	—	—
2/5/2014		1,699	1,700 ⁽ⁱⁱ⁾	21.30	2/5/2024	—	—	—	—
2/5/2014		3,092	3,093 ⁽ⁱⁱ⁾	21.30	2/5/2024	—	—	—	—
2/6/2015		1,860	5,583 ⁽ⁱⁱⁱ⁾	22.32	2/6/2025	—	—	—	—
2/5/2016		—	10,329 ^(iv)	21.06	2/5/2026	—	—	—	—
11/11/2016		—	48,846 ^(v)	26.98	11/11/2026	18,533 ⁽ⁱ⁾	484,082	—	—
Ms. Wat	2/6/2015	6,765	20,298 ⁽ⁱⁱⁱ⁾	22.32	2/6/2025	—	—	—	—
	3/25/2015	8,077	24,232 ^(vi)	23.90	3/25/2025	—	—	—	—
	1/4/2016	—	—	—	—	18,751 ⁽ⁱⁱ⁾	489,779	—	—
	2/5/2016	—	41,316 ^(iv)	21.06	2/5/2026	—	—	—	—
	11/11/2016	—	48,846 ^(v)	26.98	11/11/2026	18,533 ⁽ⁱ⁾	484,082	—	—
Ms. Lo	2/4/2011	12,056	—	14.88	2/4/2021	—	—	—	—
	2/8/2012	14,718	—	19.46	2/8/2022	—	—	—	—
	2/6/2013	10,100	3,367 ⁽ⁱ⁾	19.00	2/6/2023	—	—	—	—
	2/5/2014	—	10,195 ^(vii)	21.30	2/5/2024	—	—	—	—
	2/5/2014	6,797	6,798 ⁽ⁱⁱ⁾	21.30	2/5/2024	—	—	—	—
	2/6/2015	3,382	10,149 ⁽ⁱⁱⁱ⁾	22.32	2/6/2025	—	—	—	—
	1/4/2016	—	—	—	—	18,751 ⁽ⁱⁱ⁾	489,779	—	—
	2/5/2016	—	17,215 ^(iv)	21.06	2/5/2026	—	—	—	—
	11/11/2016	—	24,423 ^(v)	26.98	11/11/2026	9,267 ⁽ⁱ⁾	242,054	—	—
	Ms. Ng	2/8/2012	5,213	—	19.46	2/8/2022	—	—	—
2/8/2012		13,901	—	19.46	2/8/2022	—	—	—	—
2/6/2013		10,100	3,367 ⁽ⁱ⁾	19.00	2/6/2023	—	—	—	—
2/5/2014		6,116	6,118 ⁽ⁱⁱ⁾	21.30	2/5/2024	—	—	—	—
2/6/2015		2,875	8,627 ⁽ⁱⁱⁱ⁾	22.32	2/6/2025	—	—	—	—
1/4/2016		—	—	—	—	18,751 ⁽ⁱⁱ⁾	489,779	—	—
2/5/2016		—	11,706 ^(iv)	21.06	2/5/2026	—	—	—	—
11/11/2016		—	24,423 ^(v)	26.98	11/11/2026	9,267 ⁽ⁱ⁾	242,054	—	—

- (1) The actual vesting dates for unexercisable options are as follows:
 - (i) Remainder of the unexercisable award will vest on February 6, 2017.
 - (ii) One-half of the unexercisable award will vest on each of February 5, 2017 and 2018.
 - (iii) One-third of the unexercisable award will vest on each of February 6, 2017, 2018 and 2019.
 - (iv) One-fourth of the unexercisable award will vest on each of February 5, 2017, 2018, 2019 and 2020.
 - (v) One-fourth of the unexercisable award will vest on each of November 11, 2017, 2018, 2019 and 2020.
 - (vi) One-third of the unexercisable award will vest on each of March 25, 2017, 2018 and 2019.
 - (vii) 100% of the unexercisable award will vest on February 5, 2018.
- (2) The RSUs reported in this column include additional RSUs received with respect to dividends and which remain subject to the same underlying vesting conditions. The actual vesting dates for unvested RSUs are as follows:
 - (i) The RSUs vest 50% on each of November 11, 2018 and 2019.
 - (ii) The RSUs vest 25% on each of January 4, 2017 and 2018 and 50% on January 4, 2019.
- (3) The market value of these awards are calculated by multiplying the number of shares covered by the award by \$26.12, the closing price of the Company's stock on the NYSE on December 30, 2016.

2016 OPTION/SAR EXERCISES AND STOCK VESTED

The table below shows the number of shares of YUM common stock acquired during 2016 upon exercise of SAR awards and before payment of applicable withholding taxes and broker commissions. None of the NEOs exercised any SARs or received shares upon vesting of any equity awards with respect to the Company.

Name	Option/SAR Awards		Stock Awards	
	Number of Shares Acquired on Exercise (#)	Value Realized on Exercise (\$)	Number of Shares Acquired on Vesting (#)	Value realized on Vesting (\$)
(a)	(b)	(c)	(d)	(e)
Mr. Pant	91,228	8,210,621	—	—
Mr. Stedem	—	—	—	—
Ms. Wat	—	—	—	—
Ms. Lo	32,199	2,778,974	—	—
Ms. Ng	8,920	788,217	—	—

Nonqualified Deferred Compensation

During 2016, Messrs. Pant and Stedem were the only NEOs who participated in the YCHLRP, an unfunded, unsecured deferred, account-based plan maintained by the Company. The YCHLRP provides an annual allocation to the account of Messrs. Pant and Stedem equal to 20% and 8%, respectively, of their respective salary plus target bonus. In connection with the spin-off, the obligations under the YUMLRP with respect to employees continuing with the Company following the spin-off were transferred to the YCHLRP, the terms of which are substantially similar to the terms of the YUMLRP.

The YCHLRP provides an annual earnings credit to each participant's account based on the value of participant's account at the end of each year. Under the YCHLRP, Mr. Pant and Mr. Stedem receive an annual earnings credit equal to 5% of their account balances. The Company's contribution for 2016 is equal to 20% and 8%, respectively, of Mr. Pant's and Mr. Stedem's salary plus target bonus.

Under the YCHLRP, participants age 55 or older are entitled to a lump sum distribution of their account balance in the quarter following their separation of employment. Participants under age 55 with a vested YCHLRP benefit combined with any other deferred compensation benefits covered under Code Section 409A exceeds \$15,000, will not receive a distribution until the calendar quarter that follows the participant's 55th birthday. Distributions from the YCHLRP will not be made solely as a result of the separation and distribution.

YUM offered certain executives working in China retirement benefits under the Yum! Restaurants (Hong Kong) Limited Retirement Scheme. In connection with the spin-off, the Company adopted a substantially similar plan. Under this program, the Company provides a company funded contribution ranging from 5% to 10% of an executive's base salary. The Company's contribution for 2016 was equal to 5%, 10% and 10% of salary for Ms. Wat, Ms. Lo and Ms. Ng, respectively. Upon termination, participants will receive a lump sum equal to a percentage of the Company's contributions inclusive of investment return. This percentage is based on a vesting schedule that provides participants with a vested 30% interest upon completion of a minimum of three years of service, and an additional 10% vested interest for each additional completed year, up to a maximum of 100%. Participants may elect a variety of mutual funds in which to invest their account balances under the plan.

2016 NONQUALIFIED DEFERRED COMPENSATION TABLE

Name	Executive Contributions in Last FY (\$)	Registrant Contributions in Last FY (\$) ⁽¹⁾	Aggregate Earnings in Last FY (\$) ⁽²⁾	Aggregate Withdrawals/ Distributions (\$)	Aggregate Balance at Last FYE (\$) ⁽³⁾
	(a)	(b)	(c)	(d)	(e)
Mr. Pant	—	456,608	140,294	—	3,374,907
Mr. Stedem	—	79,366	503	—	37,492
Ms. Wat	—	31,356	—	—	69,415 ⁽⁴⁾
Ms. Lo	—	36,861	—	—	380,225 ⁽⁴⁾
Ms. Ng	—	36,941	—	—	454,035 ⁽⁴⁾

- (1) Amounts in this column primarily reflect allocations to the YUMLRP and the YCHLRP for Messrs. Pant and Stedem and allocations to the Bai Sheng Restaurants (Hong Kong) Limited Retirement Scheme for Mses. Wat, Lo and Ng.
- (2) Amounts in this column reflect earnings during the last fiscal year on amounts deferred under the YCHLRP. All earnings for Messrs. Pant and Stedem are based on the earnings credit provided under the YCHLRP described in the narrative above this table. For Messrs. Pant and Stedem, of the earnings reflected in this column, \$63,974 and \$229, respectively, was deemed above market earnings accruing to their accounts under the YCHLRP. For above market earnings on nonqualified deferred compensation, see the “Change in Pension Value and Nonqualified Deferred Compensation Earnings” column of the Summary Compensation Table. Under the Hong Kong Data Privacy Act, the administrator of the Bai Sheng Restaurants (Hong Kong) Limited Retirement Scheme is restricted from disclosing individual account balances under that plan and, accordingly, the Company is unable to compile earnings information with respect to this plan. Under the terms of the plan, participants may elect a variety of mutual funds in which to invest their account balances under the plan.
- (3) The amount reflected in this column is the year-end balance for Messrs. Pant and Stedem under the YCHLRP and the estimated year-end balances for Mses. Wat, Lo and Ng under the Bai Sheng Restaurants (Hong Kong) Limited Retirement Scheme.
- (4) This amount represents the aggregate amount of the Company’s contributions, exclusive of investment returns. See note (2) to this table for further information regarding investment returns with respect to the Bai Sheng Restaurants (Hong Kong) Limited Retirement Scheme. This amount was denominated in Hong Kong dollars and was converted to U.S. dollars using an exchange rate of 7.7580 for disclosure purposes.

Potential Payments Upon a Termination or a Change in Control

YCHLRP. Under the YCHLRP, participants age 55 are entitled to a lump sum distribution of their account balance following their termination of employment. Participants under age 55 who terminate with more than five years of service will receive their account balance at their 55th birthday. In case of termination of employment as of December 31, 2016, Mr. Pant and Mr. Stedem would have received \$3,374,907 and \$37,492, respectively.

Life Insurance Benefits. For a description of the supplemental life insurance plans that provide coverage to the YUM executive officers, see the All Other Compensation Table above. If Mr. Pant had died on December 31, 2016, the survivors of Mr. Pant would have received Company-paid life insurance of \$1,790,000 under this arrangement.

Severance and Change in Control Arrangements. As of December 31, 2016, the Company was not a party to any severance or change in control agreements, other than statutory requirements, entitling any of the NEOs to severance benefits upon a termination or a change in control. Under the terms of our equity agreements, all outstanding stock options and/or SARs would fully and immediately vest following a change in control if the executive is employed on the date of the change in control of the Company and is involuntarily terminated (other than for cause) on or within two years following the change in control.

In addition, Mr. Pant is subject to a letter of understanding with the Company that specifies that any post-spin-off equity awards from the Company will be eligible for continued vesting upon retirement provided Mr. Pant (i) is actively employed for at least one year following the grant date, (ii) provides at least six months notification of intention to retire and (iii) signs non-solicitation and non-compete agreements. For any awards where these three conditions are not met, and for awards issued from YUM prior to his employment with the Company, the awards will be treated with the standard provisions provided for retirement in the underlying award agreements. The letter of understanding also provides that Mr. Pant's unvested awards from YUM will continue to vest during his employment with the Company and, upon his separation from the Company, Mr. Pant will be treated as a retiree from YUM and his vested SARs can be held until the term expires and he will receive pro-rated vesting of his unvested SARs.

If a change in control and the involuntary termination of one of the Company's NEOs had occurred as of December 31, 2016, the payments or other benefits set forth below would have been made or become available to them.

	<u>Pant \$</u>	<u>Stedem \$</u>	<u>Wat \$</u>	<u>Lo \$</u>	<u>Ng \$</u>
Accelerated Vesting of SARs	1,663,873	118,946	339,986	231,553	145,477
Accelerated Vesting of RSUs	1,452,194	484,082	973,861	731,833	731,833
TOTAL	3,116,067	603,028	1,313,847	963,386	877,310

In addition, if a change in control of the Company had occurred as of December 31, 2016, the NEOs would have been entitled to receive the accelerated vesting of their equity awards with respect to YUM, with the value of such awards as follows: Mr. Pant – \$4,506,638; Mr. Stedem – \$263,442; Ms. Wat – \$949,669; Ms. Lo – \$628,306; and Ms. Ng – \$394,462.

2016 DIRECTOR COMPENSATION

The Company primarily uses stock-based compensation to attract and retain qualified candidates to serve on the Board. In setting director compensation, the Board considers the significant amount of time that directors expend in fulfilling their duties to the Company as well as the skill level required by the Company of members of the Board. The Nominating and Governance Committee of the Board reviews and makes recommendations to the Board with respect to the compensation and benefits of directors on an annual basis.

Non-Employee Directors Annual Compensation. Our non-employee directors are each compensated with an annual retainer equal to \$225,000, payable in Company common stock or, if requested by a director, up to one-half in cash. These retainers were paid in late 2016 to compensate the directors for their service from November 1, 2016 through October 31, 2017.

Chairman and Committee Chairperson Retainer. In addition to the annual equity retainer paid to all non-employee directors, the Chairman of the Board (Dr. Hu in 2016) receives an additional annual cash retainer of \$225,000. The Chairperson of the Audit Committee (Mr. Hsieh in 2016) receives an additional \$20,000 stock retainer annually, the Chairperson of the Compensation Committee (Mr. Etedgui in 2016) receives an additional \$15,000 stock retainer annually, and the Chairperson of the Nominating and Governance Committee (Dr. Hu in 2016) receives an additional \$10,000 stock retainer annually. These retainers were paid in late 2016 to compensate the directors for their service from November 1, 2016 through October 31, 2017.

Employee Directors. Employee directors do not receive additional compensation for serving on the Board of Directors.

The table below summarizes compensation paid to each non-employee director during 2016.

Name	Fees Earned or Paid in Cash(\$) ⁽¹⁾	Stock Awards (\$) ⁽²⁾	Option/SAR Awards (\$) ⁽³⁾	Total (\$)
Peter A. Bassi	112,520	112,480	—	225,000
Christian L. Campbell	14	224,986	—	225,000
Ed Yiu-Cheong Chan	14	224,986	—	225,000
Edouard Etedgui	112,520	127,480	—	240,000
Louis T. Hsieh	22	244,978	—	245,000
Fred Hu	225,004	234,996	—	460,000
Jonathan S. Linen	14	224,986	—	225,000
Ruby Lu	14	224,986	—	225,000
Zili Shao	112,520	112,480	—	225,000

- (1) Represents the portion of the annual retainer that the director elected to receive in cash rather than equity with respect to Messrs. Bassi, Etedgui and Shao, cash fees received in lieu of fractional shares in the case of Messrs. Campbell, Chan, Hsieh and Linen and Ms. Lu and the annual cash retainer paid to Dr. Hu as Chairman of the Board.
- (2) Represents the grant date fair value for annual stock retainer awards granted in 2016. Each director received shares of Company common stock determined by dividing the applicable annual retainer by the closing market price of a share of Company common stock on the date of grant, with any fractional shares paid in cash rather than equity.
- (3) At December 31, 2016, the aggregate number of SARs outstanding for each non-employee director are set forth in the following table. These SARs were received by the applicable non-employee directors in connection with the adjustment of their outstanding YUM equity awards.

Name	SARs
Peter A. Bassi	—
Christian L. Campbell	167,415
Ed Yiu-Cheong Chan	—
Edouard Etedgui	—
Louis T. Hsieh	—
Fred Hu	—
Jonathan S. Linen	26,407
Ruby Lu	—
Zili Shao	—

Stock Ownership Requirements. We expect that directors should own a meaningful number of shares of Company common stock and that a director will not sell any shares received as director compensation until at least 12 months following the director’s retirement or departure from the Board.

EQUITY COMPENSATION PLAN INFORMATION

The following table summarizes, as of December 31, 2016, the equity compensation we may issue to our directors, officers, employees and other persons under the Company's Long Term Incentive Plan, which was approved by YUM as the Company's sole stockholder prior to the spin-off.

Plan Category	Number of Securities to be Issued Upon Exercise of Outstanding Options, Warrants and Rights	Weighted- Average Exercise Price of Outstanding Options, Warrants and Rights	Number of Securities Remaining Available For Future Issuance Under Equity Compensation Plans (Excluding Securities Reflected in Column (a))
	(a)	(b)	(c)
Equity compensation plans approved by security holders	29,736,515 ⁽¹⁾	17.88 ⁽²⁾	13,467,830
Equity compensation plans not approved by security holders	—	—	—
TOTAL	29,736,515	17.88	13,467,830

- (1) Represents shares issuable upon the exercise or vesting of stock appreciation rights, restricted stock units (including dividend equivalent units), stock options and executive income deferral awards outstanding as of December 31, 2016.
- (2) Restricted stock units and executive income deferral awards do not have an exercise price. Accordingly, this amount represents the weighted-average exercise price of outstanding stock appreciation rights and stock options.

AUDIT COMMITTEE REPORT

Who serves on the Audit Committee of the Board of Directors?

The members of the Audit Committee are Louis T. Hsieh (Chair), Peter A. Bassi, Ed Yiu-Cheong Chan and Ruby Lu. The Board of Directors has determined that all of the members of the Audit Committee are independent within the meaning of applicable SEC regulations and the listing standards of the NYSE and that Mr. Hsieh, the Chairperson of the Audit Committee, is qualified as an audit committee financial expert within the meaning of SEC regulations. The Board has also determined that Mr. Hsieh has accounting and related financial management expertise within the meaning of the listing standards of the NYSE and that each member of the Audit Committee is financially literate within the meaning of the NYSE listing standards.

What document governs the activities of the Audit Committee?

The Audit Committee operates under a written charter adopted by the Board of Directors. The Audit Committee's responsibilities are set forth in the charter. The Audit Committee annually reviews and reassesses the adequacy of its charter and recommends any proposed changes to the Board for approval. The charter is available on our website at ir.yumchina.com.

What are the responsibilities of the Audit Committee?

The Audit Committee assists the Board in fulfilling its responsibilities for general oversight of the integrity of the Company's financial statements, the adequacy of the Company's system of internal controls and procedures and disclosure controls and procedures, the Company's risk management, the Company's compliance with legal and regulatory requirements, the independent auditor's qualifications and independence and the performance of the Company's internal audit function and independent auditor. The Audit Committee has the authority to obtain advice and assistance from independent legal, accounting or other advisors as the Audit Committee deems necessary or appropriate to carry out its duties and receive appropriate funding, as determined by the Audit Committee, from the Company for such advice and assistance.

The Audit Committee has sole authority to appoint, determine funding for or replace the independent auditor and manages the Company's relationship with its independent auditor, which reports directly to the Audit Committee. Each year, the Audit Committee evaluates the performance, qualifications and independence of the independent auditor. In doing so, the Audit Committee considers whether the independent auditor's quality controls are adequate and the provision of permitted non-audit services is compatible with maintaining the auditor's independence, taking into account the opinions of management and internal auditor.

The members of the Audit Committee meet periodically in separate executive sessions with management (including the Company's Chief Financial Officer and Principal Accounting Officer), the internal auditors and the independent auditor, and have such other direct and independent interaction with such persons from time to time as the members of the Audit Committee deem appropriate. The Audit Committee may request any officer or employee of the Company or the Company's outside counsel or independent auditor to attend a meeting of the Audit Committee or to meet with any members of, or consultants to, the Audit Committee.

What matters have members of the Audit Committee discussed with management and the independent auditor?

As part of its oversight of the Company's financial statements, the Audit Committee reviews and discusses with both management and the Company's independent auditor all annual and quarterly financial statements prior to their issuance. During 2016, management advised the Audit Committee that each set of financial statements reviewed had been prepared in accordance with accounting principles generally accepted in the U.S. and reviewed significant accounting and disclosure issues with the Audit Committee. These reviews included discussions with the independent auditor of matters required to be discussed pursuant to Public Company Accounting Oversight Board ("**PCAOB**") Auditing Standard No. 16 (*Communication with Audit Committees*), including the quality (not merely

the acceptability) of the Company's accounting principles, the reasonableness of significant judgments, the clarity of disclosures in the financial statements and disclosures related to critical accounting practices. The Audit Committee has also discussed with KPMG Huazhen LLP matters relating to its independence, including a review of audit and non-audit fees and the written disclosures and letter received from KPMG Huazhen LLP required by applicable requirements of the PCAOB regarding KPMG Huazhen LLP's communications with the Audit Committee concerning independence. The Audit Committee also considered whether non-audit services provided by the independent auditor are compatible with the independent auditor's independence. The Audit Committee also received regular updates, and written summaries as required by the PCAOB rules (for tax and other services), on the amount of fees and scope of audit, audit-related, tax and other services provided.

In addition, the Audit Committee reviewed key initiatives and programs aimed at strengthening the effectiveness of the Company's internal and disclosure control structure. As part of this process, the Audit Committee monitored the scope and adequacy of the Company's internal auditing program, reviewing staffing levels and steps taken to implement recommended improvements in internal procedures and controls. The Audit Committee also reviewed and discussed legal and compliance matters with management, and, as necessary or advisable, the Company's independent auditor.

Has the Audit Committee made a recommendation regarding the audited financial statements for fiscal 2016?

Based on the Audit Committee's discussions with management and the independent auditor and the Audit Committee's review of the representations of management and the report of the independent auditor to the Board of Directors, and subject to the limitations on the Audit Committee's role and responsibilities referred to above and in the Audit Committee Charter, the Audit Committee recommended to the Board of Directors that it include the audited consolidated financial statements in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2016 for filing with the SEC.

Who prepared this report?

This report has been furnished by the members of the Audit Committee:

Louis T. Hsieh, Chairperson
Peter A. Bassi
Ed Yiu-Cheong Chan
Ruby Lu

ADDITIONAL INFORMATION

Who pays the expenses incurred in connection with the solicitation of proxies?

Expenses in connection with the solicitation of proxies will be paid by us. Proxies are being solicited principally by mail, by telephone and through the Internet. We have retained Georgeson Inc. to act as a proxy solicitor for a fee estimated to be \$14,500, plus reimbursement of out-of-pocket expenses. In addition, our directors, officers and regular employees, without additional compensation, may solicit proxies personally, by e-mail, telephone, fax or special letter. We will reimburse brokerage firms and others for their expenses in forwarding proxy materials to the beneficial owners of shares of Company common stock.

How may I elect to receive stockholder materials electronically and discontinue my receipt of paper copies?

Stockholders with shares registered directly in their name who received stockholder materials in the mail may elect to receive future annual reports and proxy statements from us and to vote their shares through the Internet instead of receiving copies through the mail. We are offering this service to provide stockholders with added convenience, to reduce our environmental impact and to reduce annual report printing and mailing costs.

To elect this option, go to www.amstock.com, click on Stockholder Account Access, log in and locate the option to receive Company mailings via e-mail. Stockholders who elect this option will be notified by mail how to access the proxy materials and how to vote their shares on the Internet or by phone.

If you consent to receive future proxy materials electronically, your consent will remain in effect unless it is withdrawn by writing our transfer agent, American Stock Transfer and Trust Company, LLC, 6201 15th Avenue, Brooklyn, NY 11219 or by logging onto our transfer agent's website at www.amstock.com and following the applicable instructions. Also, while this consent is in effect, if you decide you would like to receive a paper copy of the proxy materials, you may call, write or e-mail American Stock Transfer and Trust Company, LLC or Yum China Holdings, Inc., 7100 Corporate Drive, Plano, Texas 75024, or Yum China Holdings, Inc., 16/F Two Grand Gateway, 3 Hong Qiao Road, Shanghai 200030 People's Republic of China, Attention: Corporate Secretary.

I share an address with another stockholder, and we received only one paper copy of the proxy materials. How may I obtain an additional copy of the proxy materials?

The Company has adopted a procedure called "householding," which has been approved by the SEC. The Company and some brokers household proxy materials, delivering a single Notice and, if applicable, this proxy statement and the annual report, to multiple stockholders sharing an address unless contrary instructions have been received from the affected stockholders or they participate in electronic delivery of proxy materials. Stockholders who participate in householding will continue to access and receive separate proxy cards. This process will help reduce our printing and postage fees, as well as save natural resources. If at any time you no longer wish to participate in householding and would prefer to receive a separate proxy statement, or if you are receiving multiple copies of the proxy statement and wish to receive only one, please notify your broker if your shares are held in a brokerage account or us if you hold registered shares. You can notify us by sending a written request to Yum China Holdings, Inc., 7100 Corporate Drive, Plano, Texas 75024, or to Yum China Holdings, Inc., 16/F Two Grand Gateway, 3 Hong Qiao Road, Shanghai 200030 People's Republic of China, Attention: Investor Relations.

May I propose actions for consideration at next year's annual meeting of the Company's stockholders or nominate individuals to serve as directors?

Under the rules of the SEC, if a stockholder wants us to include a proposal in our proxy statement and proxy card for presentation at the 2018 annual meeting of the Company's stockholders, the proposal must be received by our Corporate Secretary at our principal executive offices, Yum China Holdings, Inc., 7100 Corporate Drive, Plano, Texas 75024, or Yum China Holdings, Inc., 16/F Two Grand Gateway, 3 Hong Qiao Road, Shanghai 200030 People's Republic of China, by November 17, 2017. We strongly encourage any stockholder interested in submitting a proposal to contact our Chief Legal Officer in advance of this deadline to discuss the proposal. Stockholders may want to consult knowledgeable counsel with regard to the detailed requirements of applicable securities laws. Submitting a proposal does not guarantee that we will include it in our proxy statement.

Under our amended and restated bylaws, stockholders may also nominate persons for election as directors at an annual meeting or introduce an item of business that is not included in our proxy statement. These procedures provide that nominations for director nominees and/or an item of business to be introduced at an annual meeting must be submitted in writing to our Corporate Secretary at our principal executive offices, and the stockholder submitting any such nomination or item of business must include information set forth in our amended and restated bylaws. For the 2018 annual meeting of the Company's stockholders, we must receive the notice of your intention to introduce a nomination or to propose an item of business no earlier than December 29, 2017 and no later than January 28, 2018, unless we hold the 2018 annual meeting before March 29, 2018 or after May 28, 2018. Stockholders must also satisfy the other requirements specified in our amended and restated bylaws. You may contact the Company's Corporate Secretary at the address mentioned above for a copy of the relevant bylaw provisions regarding the requirements for making stockholder proposals and nominating director candidates.

Is any other business expected to be conducted at the Annual Meeting?

The Board is not aware of any matters that are expected to come before the Annual Meeting other than those referred to in this proxy statement. If any other matter should come before the Annual Meeting, the individuals named on the form of proxy intend to vote the proxies in accordance with their best judgment.

The chairman of the Annual Meeting may refuse to allow the transaction of any business, or to acknowledge the nomination of any person, not made in compliance with the foregoing procedures.

YUM CHINA HOLDINGS, INC.
 7100 CORPORATE DRIVE
 PLANO, TX 75024

VOTE BY INTERNET - www.proxyvote.com

Use the Internet to transmit your voting instructions and for electronic delivery of information up until at 11:59 P.M. (local time) the day before the meeting date. Have your proxy card in hand when you access the web site and follow the instructions to obtain your records and to create an electronic voting instruction form.

ELECTRONIC DELIVERY OF FUTURE PROXY MATERIALS

If you would like to reduce the costs incurred by our company in mailing proxy materials, you can consent to receiving all future proxy statements, proxy cards and annual reports electronically via e-mail or the Internet. To sign up for electronic delivery, please follow the instructions above to vote using the Internet and, when prompted, indicate that you agree to receive or access proxy materials electronically in future years.

VOTE BY PHONE - 1-800-690-6903

Use any touch-tone telephone to transmit your voting instructions up until 11:59 P.M. (local time) the day before the meeting date). Have your proxy card in hand when you call and then follow the instructions.

VOTE BY MAIL

Mark, sign and date your proxy card and return it in the postage-paid envelope we have provided or return it to Vote Processing, c/o Broadridge, 51 Mercedes Way, Edgewood, NY 11717.

TO VOTE, MARK BLOCKS BELOW IN BLUE OR BLACK INK AS FOLLOWS:

KEEP THIS PORTION FOR YOUR RECORDS
 DETACH AND RETURN THIS PORTION ONLY

THIS PROXY CARD IS VALID ONLY WHEN SIGNED AND DATED.

The Board of Directors recommends you vote FOR the following:

1. Election of Directors

Nominees	For	Against	Abstain
1a. Peter A. Bassi	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
1b. Ed Yiu-Cheong Chan	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
1c. Edouard Ettedgui	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

The Board of Directors recommends you vote FOR proposals 2 and 3.

	For	Against	Abstain
2. Ratification of Independent Auditor	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
3. Advisory Vote to Approve Executive Compensation	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

The Board of Directors recommends you vote 1 YEAR on the following proposal:

	1 year	2 years	3 years	Abstain
4. Advisory Vote on the Frequency of the Advisory Vote on Executive Compensation	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

NOTE: The proxies are authorized to vote in their discretion upon such other business as may properly come before the meeting or any adjournment or postponement thereof.

Please sign exactly as your name(s) appear(s) hereon. When signing as attorney, executor, administrator, or other fiduciary, please give full title as such. Joint owners should each sign personally. All holders must sign. If a corporation or partnership, please sign in full corporate or partnership name, by authorized officer.

--	--

Signature [PLEASE SIGN WITHIN BOX] Date

--	--

Signature (Joint Owners) Date

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Important Notice Regarding the Availability of Proxy Materials for the Annual Meeting: The Notice & Proxy Statement, Form 10-K is/are available at www.proxyvote.com

**YUM CHINA HOLDINGS, INC.
Annual Meeting of Stockholders
April 28, 2017 8:30 AM
This proxy is solicited by the Board of Directors**

The undersigned stockholder(s) hereby appoint(s) Shella Ng and Ted Stedem, or either of them, as proxies, each with the power to appoint his/her substitute, revoking all proxies previously given, and hereby authorize(s) them to represent and to vote, as designated on the reverse side of this proxy, all of the shares of common stock of Yum China Holdings, Inc. that the stockholder(s) is/are entitled to vote at the Annual Meeting of Stockholders to be held at 8:30 a.m. local time, on April 28, 2017, at the Mandarin Oriental Hong Kong, 5 Connaught Road, Central, Hong Kong, and any adjournment or postponement thereof.

This proxy, when properly executed, will be voted in the manner directed herein. If no such direction is made, this proxy will be voted in accordance with the Board of Directors' recommendations.

Continued and to be signed on reverse side

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

FORM 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934 for the fiscal year ended December 31, 2016

OR

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

For the transition period from _____ to _____

Commission file number 001-37762

Yum China Holdings, Inc.

(Exact Name of Registrant as Specified in Its Charter)

Delaware
(State or Other Jurisdiction of
Incorporation or Organization)

7100 Corporate Drive
Plano, Texas 75024
United States of America

81-2421743
(I.R.S. Employer
Identification No.)

16/F Two Grand Gateway
3 Hong Qiao Road
Shanghai 200030
People's Republic of China

(Address, including Zip Code, of Principal Executive Offices)

Registrant's telephone number, including area code: (972) 338-7530

Securities registered pursuant to Section 12(b) of the Act:

<u>Title of Each Class</u>	<u>Name of Each Exchange on Which Registered</u>
Common Stock, par value \$0.01 per share	New York Stock Exchange
Preferred Share Purchase Rights	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act:

None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ___ No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes ___ No

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

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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 definitions of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act (Check one): Large accelerated filer: Accelerated filer: Non-accelerated filer: Smaller reporting company:

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

As of May 31, 2016, the last business day of the registrant's most recently completed second fiscal quarter, the registrant's common stock was not traded on any exchange or over-the-counter market. The number of shares outstanding of the registrant's common stock as of February 28, 2017 was 384,311,143 shares.

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DOCUMENTS INCORPORATED BY REFERENCE

Portions of the definitive proxy statement for the registrant's 2017 annual meeting of stockholders (the "2017 Proxy Statement"), to be filed not later than 120 days after the end of the registrant's fiscal year, are incorporated by reference into Part III of this Form 10-K.

Forward-Looking Statements

This annual report on Form 10-K (this “Form 10-K”) includes “forward-looking statements” within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended (referred to herein as “Exchange Act”). We intend all forward-looking statements to be covered by the safe harbor provisions of the Private Securities Litigation Reform Act of 1995.

Forward-looking statements can be identified by the fact that they do not relate strictly to historical or current facts. These statements often include words such as “may,” “will,” “estimate,” “intend,” “seek,” “expect,” “project,” “anticipate,” “believe,” “plan,” “could,” “target,” “predict,” “likely,” “should,” “forecast,” “outlook,” “model,” “continue,” “ongoing” or other similar terminology. Forward-looking statements are based on our current expectations, estimates, assumptions or projections concerning future results or events, including, without limitation, statements regarding our new store development plans, growth and margin expansion opportunities, expected franchisee ownership mix and benefits from VAT reform. Forward-looking statements are neither predictions nor guarantees of future events, circumstances or performance and are inherently subject to known and unknown risks, uncertainties and assumptions that could cause our actual results and events to differ materially from those indicated by those forward-looking statements. We cannot assure you that any of our expectations, estimates, assumptions or projections will be achieved. Factors that could cause actual results and events to differ materially from our expectations, estimates, assumptions or projections include (i) the risks and uncertainties described in the Risk Factors included in Part I, Item 1A of this Form 10-K and (ii) the factors described in Management’s Discussion and Analysis of Financial Condition and Results of Operations included in Part II, Item 7 of this Form 10-K. You should not place undue reliance on forward-looking statements, which speak only as of the date hereof. We disclaim any obligation to publicly update any forward-looking statement to reflect subsequent events or circumstances, except as required by law.

PART I

Item 1. Business.

Yum China Holdings, Inc. (referred to herein as “Yum China” and, together with its subsidiaries the “Company,” “we,” “us,” and “our”) was incorporated in Delaware on April 1, 2016. The Company’s U.S. office is located at 7100 Corporate Drive, Plano, Texas, 75024, which carries on the key book-keeping, record-keeping and day-to-day management functions of the holding company, and the telephone number at that location is (972) 338-7530. The Company’s operational headquarters is located at 16/F Two Grand Gateway, 3 Hong Qiao Road, Shanghai, 200030, People’s Republic of China (the “PRC” or “China”), where its senior management team is based. Our website address is <http://www.yumchina.com>. The reference to the Company’s website address is for informational purposes only, does not constitute incorporation by reference of the information contained on the website and should not be considered part of this Form 10-K.

“U.S. dollars”, “\$” or “US\$” refers to the legal currency of the United States, and “RMB” or “Renminbi” refers to the legal currency of China.

References to “our” or “the Company’s” restaurants or restaurant system include references to restaurants owned or franchised by us.

Spin-off Transaction

The Company separated from Yum! Brands, Inc. (“YUM” or the “Parent”) on October 31, 2016 (the “separation”), becoming an independent, publicly traded company as a result of a pro rata distribution (the “distribution”) of all outstanding shares of Yum China common stock to shareholders of YUM. On October 31, 2016, YUM’s shareholders of record as of 5:00 p.m. Eastern Time on October 19, 2016 received one share of Yum China common stock for every one share of YUM common stock held as of the record date. Yum China’s common stock began trading “regular way” under the ticker symbol “YUMC” on the New York Stock Exchange on November 1, 2016.

In connection with the separation of the Company from YUM, Yum! Restaurants Asia Pte. Ltd. (“YRAPL”), a wholly-owned indirect subsidiary of YUM, and Yum Restaurants Consulting (Shanghai) Company Limited (“YCCL”), a wholly-owned indirect subsidiary of Yum China, entered into a 50-year master license agreement with automatic renewals for additional consecutive renewal terms of 50 years each, subject only to YCCL being in “good standing” and unless YCCL gives notice of its intent not to renew, for the exclusive right to use and sublicense the use of intellectual property owned by YUM and its subsidiaries for the development, promotion and operation of the KFC, Pizza Hut and, subject to achieving certain agreed upon milestones, Taco Bell brands and their related marks and other intellectual property rights for restaurant services in the PRC, excluding Hong Kong, Taiwan and Macau. In exchange, we pay a license fee to YUM equal to 3% of net system sales from both our Company and franchise restaurants. We own the East Dawning and Little Sheep intellectual property and pay no license fee related to these concepts.

The KFC, Pizza Hut, East Dawning, Little Sheep and Taco Bell brands are collectively referred to as the “brands.” The KFC, Pizza Hut Casual Dining, Pizza Hut Home Service, East Dawning, Little Sheep and Taco Bell concepts are collectively referred to as the “Concepts.” Throughout this Form 10-K, the terms “restaurants,” “stores” and “units” are used interchangeably.

General

We are the largest restaurant company in China, with over 7,500 restaurants as of year-end 2016, and \$6.8 billion of revenue, net income of \$502 million and \$1.13 billion of adjusted EBITDA in 2016. Our growing restaurant base consists of China's leading restaurant concepts, including KFC, Pizza Hut Casual Dining, Pizza Hut Home Service, East Dawning, Little Sheep and Taco Bell. We have the exclusive right to operate and sub-license the KFC, Pizza Hut and Taco Bell brands in China, and own the East Dawning and Little Sheep concepts outright. We were the first major global restaurant brand to enter China in 1987 and we have developed deep experience operating in the market. We have since grown to become one of China's largest retail developers covering over 1,100 cities and opening an average of two new locations per day over the past five years.

As of December 31, 2016, we owned and operated approximately 90% of our restaurants. Franchisees contribute to our revenues on an ongoing basis through the payment of royalties based on a percentage of sales. KFC is the leading quick-service restaurant ("QSR") brand in China in terms of system sales and number of restaurants. As of December 31, 2016, KFC operated over 5,200 restaurants in over 1,100 cities across China. Measured by number of restaurants, we believe KFC has a two-to-one lead over the nearest Western QSR competitor in China and KFC continues to grow in both large and small cities. Similarly, Pizza Hut Casual Dining is the leading casual dining restaurant ("CDR") concept in China as measured by system sales and number of restaurants. We believe Pizza Hut Casual Dining, with over 1,700 restaurants in over 400 cities as of December 31, 2016, has an approximately six-to-one lead in terms of restaurants over its nearest Western CDR competitor in China.

Restaurant Concepts

Most restaurants in each Concept offer consumers the ability to dine in and/or carry out food. In addition, KFC, Pizza Hut Casual Dining, Pizza Hut Home Service and East Dawning offer delivery service.

Each Concept has proprietary menu items, many developed in China, and emphasizes the preparation of food with high quality ingredients, as well as unique recipes and special seasonings to provide appealing, tasty and convenient food at competitive prices.

Following is a brief description of each Concept:

KFC

KFC is the largest restaurant brand in China in terms of system sales and number of restaurants. Founded in Corbin, Kentucky by Colonel Harland D. Sanders in 1939, KFC opened its first restaurant in Beijing, China in 1987. As of December 31 2016, almost 30 years later, there were over 5,200 KFC restaurants in China, and the Company plans to continue adding new units. In addition to Original Recipe chicken, KFC in China has an extensive menu featuring pork, seafood, rice dishes, fresh vegetables, soups, congee, desserts and many other products, including premium coffee. The KFC brand is also seeking to increase revenues from its restaurants throughout the day with breakfast, delivery and 24-hour operations in many of its locations.

Pizza Hut Casual Dining

Pizza Hut Casual Dining is the largest Western CDR brand in China as measured by system sales and number of restaurants. It operates in over 400 cities and offers multiple dayparts, including breakfast and afternoon tea. The first Pizza Hut Casual Dining restaurant in China opened in 1990, and as of year-end 2016, there were over 1,700 Pizza Hut Casual Dining restaurants in China. Pizza Hut Casual Dining has an extensive menu offering a broad variety of pizzas, entrees, pasta, rice dishes, appetizers, beverages and desserts. In 2016, Pizza Hut Casual Dining was again ranked the "Most Preferred Western Casual Dining Restaurant" in China by The Nielsen Corporation.

Other Concepts

Pizza Hut Home Service. The Company introduced pizza delivery to China in 2001, and as of December 31, 2016 there were over 360 Pizza Hut Home Service units in over 50 cities in China, specializing in professional and convenient delivery of Chinese food as well as pizza. Over 80% of the brand's orders came through online or mobile channels in 2016. We believe its professional service and diverse menu provide a strong platform for continued growth in the future.

Little Sheep. A casual-dining brand with its roots in Inner Mongolia, China, Little Sheep specializes in "Hot Pot" cooking, which is very popular in China, particularly during the winter months. Little Sheep had over 240 units in both China and international markets as of December 31, 2016. Of these, over 200 units were franchised.

East Dawning. East Dawning is a Chinese food QSR brand, primarily located in large coastal cities. There were 13 restaurants as of year-end 2016. This brand is not viewed as a significant growth engine for the Company.

Taco Bell. Taco Bell is the world's leading QSR brand specializing in Mexican-style food, including tacos, burritos, quesadillas, salads, nachos and similar items. The Company opened its first Taco Bell restaurant in Shanghai, China, in December 2016.

Reportable Segments

We have two reportable segments: KFC and Pizza Hut Casual Dining. We also have four other operating segments consisting of the operations of Pizza Hut Home Service, East Dawning, Little Sheep and Taco Bell, which are combined and referred to as All Other Segments.

In the first quarter of 2017, we started discussions on integrating the management and business approach for Pizza Hut Casual Dining and Pizza Hut Home Service which allow us to create a network of approximately 2,000 stores for pizza delivery. As we make progress on implementing changes, we will continue to evaluate the impact on reportable segments.

The following table presents the total segment revenue attributable to each reportable segment for each of the last three years.

	Revenues (\$ Billions)		
	2016	2015	2014
KFC	4.7	4.8	4.9
Pizza Hut Casual Dining	1.8	1.8	1.7
All Other Segments	0.3	0.3	0.3
	<u>6.8</u>	<u>6.9</u>	<u>6.9</u>

See Note 18 to the Consolidated and Combined Financial Statements in Part II, Item 8. for additional information concerning the Company's segments.

Our Strategies

The Company's primary strategy is to grow sales and profits across its portfolio of brands through increased brand relevance, new store development and enhanced unit economics. Other areas of investment include store remodels, product innovation and quality, improved operating platforms leading to improved service, store-level human resources including recruiting and training, creative marketing programs and product testing.

New-Unit Growth

Rapidly growing consumer class. Given the rapidly expanding middle class, we believe that there is significant opportunity to expand within China, and we intend to focus our efforts on increasing our geographic footprint in both existing and new markets. We expanded our restaurant count from 4,493 units in 2011 to 7,562 units as of the end of 2016, representing a compounded annual growth rate (“CAGR”) of 11%.

Franchise opportunity. As of December 31, 2016, approximately 10% of our restaurants were operated by franchisees. Going forward, we anticipate high franchisee demand for our brands, supported by strong unit economics, operational consistency and simplicity, and multiple store types to drive restaurant growth. While the franchise market in China is still in its early stages compared to developed markets, the Company plans to continue to increase its franchisee-owned store percentage over time.

Development pipeline. We consider our development pipeline to be robust, and believe we have an opportunity to grow our restaurant count three times over the next two to three decades. For additional information on the risks associated with this growth strategy, see the section entitled “Item 1A. Risk Factors,” including the risk factor entitled “We may not attain our target development goals; aggressive development could cannibalize existing sales; and new restaurants may not be profitable.” We also believe the opportunity to expand Taco Bell restaurants and other Concepts could further increase our total unit count.

Same-Store Sales Growth

Flavor innovation. We are keenly aware of the strength of our core menu items but we also seek to continue to introduce innovative items to meet evolving consumer preferences and local tastes, while simultaneously maintaining brand relevance and broadening brand appeal. For example, KFC offers soy bean milk, fried dough sticks and congee for breakfast. In addition to breakfast, KFC has introduced rice dishes, Peking style chicken twisters, roasted chicken products, egg tarts and fresh lemon/calamansi tea.

Daypart opportunities. We believe there are significant daypart opportunities across our brands. For example, KFC introduced premium coffee to expand its breakfast and afternoon dayparts and Pizza Hut Casual Dining has focused on breakfast and afternoon tea to further grow same-store sales.

Customer frequency through mobile connectivity. KFC rolled out its K-Gold loyalty program in 2015 with the eventual goal of a fully digitized customer experience. The brand also plans to improve the customer experience through ease of ordering and speed of service, supported by innovative technology. Pizza Hut Casual Dining is a leader in providing a digital experience with its loyalty program, free in-store Wi-Fi, queue ticketing and pre-ordering, partnering with Alipay and WeChat to receive cashless payments. As of December 31, 2016, our loyalty programs have over 80 million members between KFC and Pizza Hut and are ranked #1 in the restaurant industry worldwide in terms of number of members.

Best in-store experience. The Company continuously looks for ways to improve the customer experience. For example, with continued investment in refurbishing our restaurants, over 75% of KFC’s store portfolio as of December 31, 2016 has been remodeled or built in the past five years. Pizza Hut Casual Dining is also well-regarded for offering consumers a contemporary casual dining setting. Our brands also look to improve efficiency to drive sales growth. For example, we are simplifying menu boards and fine-tuning our digital menu boards and in-store self-service order devices. We are also exploring expansion of our delivery business through online-to-offline, or O2O (known as aggregators).

Value innovation. KFC plans to continue to focus on value with product offerings such as the bucket and increased combo options throughout the day. Pizza Hut Casual Dining expects to leverage past innovations like business lunch set and breakfast to drive growth.

O2O and home delivery. China is a world leader in the emerging O2O market. This is where digital online ordering technologies interact with traditional brick and mortar retail to enhance the shopping experience. In the restaurant sector, KFC and Pizza Hut Home Service are already leading brands in home delivery in terms of online sales in China. We see considerable further growth potential in the rapidly growing in-home consumption market by aligning our proven restaurant operation capabilities with emerging specialized O2O firms, or aggregators, that offer consumers the ability to order any restaurant food at home. Pizza Hut Home Service started partnering with aggregators in 2014, followed by KFC and Pizza Hut Casual Dining in 2015. These aggregators include our restaurants in their mobile or online platforms and we generate revenue when orders placed through the platforms are delivered to the customers. We use our own staff, including outsourced riders, to deliver orders placed through aggregators' platforms to customers of KFC and Pizza Hut Home Service, while we use the aggregators' delivery services, for which we pay a commission, for Pizza Hut Casual Dining orders. For orders that are placed through the platforms, customers make payments to the aggregators through either mobile payment applications, such as WeChat and Alipay, which are managed by third-party payment processors, or cash upon delivery. For transactions with payments collected by the aggregators from customers, the aggregators settle the amount with third-party payment processors and remit the proceeds to the restaurants generally within a few business days, with limited exceptions. In 2016, approximately 10% of the Company's sales were generated from delivery. This could be an exciting new business opportunity with potential to create substantial stockholder value.

Enhanced Profitability

We focus on improving our unit-level economics and overall profits while also making the necessary investments to support our future growth. Since we increased our focus on restaurant margin improvement in late 2013, restaurant margins improved over three percentage points from 2014 to 2016. We plan to pursue additional opportunities to improve profits over the long term by continuing our focus on fiscal discipline and leveraging fixed costs, while maintaining the quality customer experience for which our brands are known.

Franchise and New Business Development

The franchise programs of the Company are designed to promote consistency and quality, and the Company is selective in granting franchisees. Franchisees supply capital – initially by paying a franchise fee to the Company and by purchasing or leasing the land use right, building, equipment, signs, seating, inventories and supplies; and, over the longer term, by reinvesting in the business through expansion. As of December 31, 2016, franchisees owned and operated about 10% of our restaurants. Franchisees contribute to the Company's revenues on an ongoing basis through the payment of royalties based on a percentage of sales.

The Company believes that it is important to maintain strong and open relationships with its franchisees and their representatives. To this end, the Company invests a significant amount of time working with the franchisees and their representative organizations on key aspects of the business, including products, equipment, operational improvements and standards and management techniques.

Restaurant Operations

Restaurant management structure varies among our brands and by unit size. Generally, each restaurant operated by the Company is led by a Restaurant General Manager (“RGM”), together with one or more Assistant Managers. RGMs are skilled and highly trained, with most having a college-level education. Each brand issues detailed manuals, which may then be customized to meet local regulations and customs. These manuals set forth standards and requirements for all aspects of restaurant operations, including food safety and quality, food handling and product preparation procedures, equipment maintenance, facility standards and accounting control procedures. The restaurant management teams are responsible for the day-to-day operation of each unit and for ensuring compliance with operating standards. The performance of RGMs is regularly monitored and coached by Area Managers. In addition, senior operations leaders regularly visit restaurants to promote adherence to system standards and mentor restaurant teams.

Supply and Distribution

The Company’s restaurants, including those operated by franchisees, are substantial purchasers of a number of food and paper products, equipment and other restaurant supplies. The principal items purchased include chicken, cheese, beef and pork products and paper and packaging materials. The Company has not experienced any significant, continuous shortages of supplies, and alternative sources for most of these products are generally available. Prices paid for these supplies fluctuate. When prices increase, the brands may attempt to pass on such increases to their customers, although there is no assurance that this can be done practically.

The Company partners with approximately 600 independent suppliers, mostly China-based, providing a wide range of products. The Company, along with multiple independently owned and operated distributors, utilizes 17 logistics centers and one consolidation center to distribute restaurant products to owned and franchised stores. The Company also owns a seasoning facility in Inner Mongolia, which supplies products to the Little Sheep business, as well as to third-party customers.

Prior to August 2016, all restaurants that operate the Company’s Concepts, including those owned by franchisees and unconsolidated affiliates, entered into purchase agreements with each of our approved third-party suppliers for raw materials with agreed pricing guidelines applicable to all entities. To improve efficiency and effectiveness of the procurement process, in August 2016, the Company adopted a central procurement model whereby the Company centrally purchases substantially all food and paper products from approved suppliers for most of the restaurants regardless of ownership and then onward sells and delivers them to most of the legal entities, including franchisees and unconsolidated affiliates, that operate the Company’s restaurants. The Company believes this central procurement model allows the Company to maintain quality control and achieves better prices and terms through volume purchases. Under the central procurement model, the materials purchased from various suppliers are intended to be sold to most of the legal entities on a cost-plus basis. The ordering process remains the same under the central procurement model except that the legal title of all materials is initially under the Company instead of the other legal entities. As a result, net inventory, receivables due from franchisees and unconsolidated affiliates, and payables due to suppliers increased as of December 31, 2016.

Food safety is the top priority at the Company. Food safety systems include rigorous standards and training of employees in our restaurants and distribution system, as well as requirements for suppliers. These standards and training topics include, but are not limited to, employee health, product handling, ingredient and product temperature management and prevention of cross contamination. Food safety training is focused on illness prevention, food safety and regulation adherence in day-to-day operations. Our standards also promote compliance with applicable laws and regulations when building new or renovating existing restaurants. For further information on food safety issues, see “Item 1A. Risk Factors—Risks Related to Our Business and Industry—Food safety and food-borne illness concerns may have an adverse effect on our reputation and business”.

Trademarks and Patents

The Company's use of certain material trademarks and service marks is governed by a master license agreement between YRAPL and YCCL. The Company is the exclusive licensee of the KFC, Pizza Hut and, subject to achieving certain agreed upon milestones, Taco Bell brands and their related marks and other intellectual property rights for restaurant services in the PRC, excluding Hong Kong, Taiwan and Macau. The term of the license is 50 years with automatic renewals for additional consecutive renewal terms of 50 years each, subject only to YCCL being in "good standing" and unless YCCL gives notice of its intent not to renew.

The Company's use of certain other material intellectual property (including intellectual property in product recipes, restaurant operation and restaurant design) is likewise governed by the master license agreement with YRAPL.

The Company owns registered trademarks and service marks relating to the East Dawning and Little Sheep brands. Collectively, these licensed and owned marks have significant value and are important to the Company's business. The Company's policy is to pursue registration of our important intellectual property rights whenever feasible and to oppose vigorously any infringement of our rights.

Working Capital

Information about the Company's working capital is included in MD&A in Part II, Item 7. and the Consolidated and Combined Statements of Cash Flows in Part II, Item 8.

Seasonality

Due to the nature of our operations, the Company has experienced higher sales during holidays and summer months.

Competition

Data from the National Bureau of Statistics of China indicates that sales in the consumer food service market in China totaled over \$500 billion in 2016. Industry conditions vary by region, with local Chinese restaurants and Western chains present, but the Company possesses the largest market share (as measured by both units and system sales). On average, competition in China is less compared to the United States, and branded QSR units per population are well below that of the United States. However, competition is increasing, and the Company still competes with respect to food quality, price, service, convenience, restaurant location and concept. The restaurant business is often affected by changes in consumer tastes; national, regional or local economic conditions; demographic trends; traffic patterns; the type, number and location of competing restaurants; and disposable income. The Company competes not only for consumers but also for management and hourly personnel and suitable real estate sites. Among KFC's primary competitors in China are restaurant chains such as McDonald's and Dicos. Pizza Hut's Western pizza-brand competitors include Domino's and Papa John's.

Research and Development ("R&D")

The Company operates a test kitchen in Shanghai, China to promote product innovation. From time to time, the Company also works with independent suppliers to conduct R&D activities for the benefit of the Company. The Company expensed \$5 million in each of 2016, 2015 and 2014 for R&D activities.

Government Regulations

The Company is subject to various laws affecting its business, including laws and regulations concerning information security, labor, health, sanitation and safety. Each of the Concepts' restaurants must comply with licensing and regulation by a number of governmental authorities, which include restaurant operation, health, sanitation, food safety, environmental protection and fire agencies in the province and/or municipality in which the restaurant is located. The Company has not historically been materially adversely affected by such licensing and regulation or by any difficulty, delay or failure to obtain required licenses or approvals. The Company is also subject to tariffs and regulations on imported commodities and equipment and laws regulating foreign investment, as well as anti-bribery and corruption laws. See "Item 1A. Risk Factors" for a discussion of risks relating to federal, state, provincial, local and international governmental regulation of our business.

Regulations Relating to Dividend Distribution

The Chinese laws, rules and regulations applicable to our China subsidiaries permit payments of dividends only out of their accumulated profits, if any, determined in accordance with applicable accounting standards and regulations. In addition, under Chinese law, an enterprise incorporated in China is required to set aside at least 10% of its after-tax profits each year, after making up previous years' accumulated losses, if any, to fund certain statutory reserve funds, until the aggregate amount of such a fund reaches 50% of its registered capital. As a result, our China subsidiaries are restricted in their ability to transfer a portion of their net assets to us in the form of dividends. At the discretion of their board of directors, as enterprises incorporated in China, our China subsidiaries may allocate a portion of their after-tax profits based on China accounting standards to staff welfare and bonus funds. These reserve funds and staff welfare and bonus funds are not distributable as cash dividends.

Regulations Relating to Taxation

Enterprise Income Tax. Under the China Enterprise Income Tax Law (the "EIT Law") and its implementation rules, a China resident enterprise is subject to Chinese enterprise income tax in respect of its net taxable income derived from sources inside and outside China. The term "resident enterprise" refers to any enterprise established in China and any enterprise established outside China with a "de facto management body" within China.

Our China subsidiaries are regarded as China resident enterprises by virtue of their incorporation in China, and are generally subject to Chinese enterprise income tax on their worldwide income at the current uniform rate of 25%, unless reduced under certain specific qualifying criteria. Our China subsidiaries may deduct reasonable expenses that are actually incurred and are related to the generation of their income, including interest and other borrowing expenses, amortization of land use rights and depreciation of buildings and certain fixed assets, subject to any restrictions that may be imposed under the EIT Law, its implementation regulations and any applicable tax notices and circulars issued by the Chinese government or tax authorities.

Yum China and each subsidiary of Yum China that is organized outside of China intends to conduct its management functions in a manner that does not cause it to be a China resident enterprise, including by carrying on its day-to-day management activities and maintaining its key records, such as resolutions of its board of directors and resolutions of stockholders, outside of China. As such, we do not believe that Yum China or any of its non-Chinese subsidiaries should be considered a China resident enterprise for purposes of the EIT Law, and should not be subject to Chinese enterprise income tax on that basis. See "Risk Factors—Risks Related to Doing Business in China—Under the EIT Law, if we are classified as a China resident enterprise for Chinese enterprise income tax purposes, such classification would likely result in unfavorable tax consequences to us and our non-Chinese stockholders."

Value-Added Tax / Business Tax and Local Surcharges. Effective on May 1, 2016, a 6% value-added tax (“VAT”) on output replaced the 5% business tax (“BT”) that has historically been applied to certain restaurant sales under the China Provisional Regulations on Business Tax. Pursuant to Circular Caishui [2016] No. 36 jointly issued by the Ministry of Finance and the State Administration of Taxation (“SAT”), beginning May 1, 2016, any entity engaged in the provision of catering services in China is generally required to pay VAT at the rate of 6% on revenues generated from the provision of such services, less any creditable VAT already paid or borne by such entity upon purchase of materials and services. Local surcharges generally ranging from 7% to 13%, varying with the location of the relevant China subsidiary, are imposed on the amount of VAT payable. On December 21, 2016, Circular Caishui [2016] No. 140 was jointly issued by the Ministry of Finance and the SAT, pursuant to which it was confirmed that an entity engaged in catering services shall pay VAT at the rate of 6% on revenues generated from the provision of take-out food.

Repatriation of Dividends from Our China Subsidiaries. Dividends (if any) paid by our China subsidiaries to their direct offshore parent company are subject to Chinese withholding income tax at the rate of 10%, provided that such dividends are not effectively connected with any establishment or place of the offshore parent company in China. The 10% withholding income tax rate may be reduced or exempted pursuant to the provisions of any applicable tax treaties or tax arrangements entered into by China. In the event that any dividend is or is deemed paid to Yum China, it is subject to U.S. federal income tax with credits for foreign taxes paid, and the utilization of foreign tax credits is subject to complex limitations.

Gains on Direct Disposal of Equity Interests in Our China Subsidiaries. Under the EIT Law and its implementation rules, gains derived by non-resident enterprises from the sale of equity interests in a China resident enterprise are subject to Chinese withholding income tax at the rate of 10%. The 10% withholding income tax rate may be reduced or exempted pursuant to applicable tax treaties or tax arrangements. The gains are computed based on the difference between the sales proceeds and the original investment basis. Stamp duty is also payable upon a direct transfer of equity interest in a China resident enterprise. The stamp duty is calculated at 0.05% on the transfer value, payable by each of the transferor and transferee. We may be subject to these taxes in the event of any future sale by us of a China resident enterprise.

Gains on Indirect Disposal of Equity Interests in Our China Subsidiaries. In February 2015, the SAT issued the SAT’s Bulletin on Several Issues of Enterprise Income Tax on Income Arising from Indirect Transfers of Property by Non-resident Enterprises (“Bulletin 7”). Pursuant to Bulletin 7, an “indirect transfer” of Chinese taxable assets, including equity interests in a China resident enterprise (“Chinese interests”), by a non-resident enterprise, may be recharacterized and treated as a direct transfer of Chinese taxable assets, if such arrangement does not have reasonable commercial purpose and the transferor avoids payment of Chinese enterprise income tax. Where a non-resident enterprise conducts an “indirect transfer” of Chinese interests by disposing of equity interests in an offshore holding company, the transferor, transferee and/or the China resident enterprise being indirectly transferred may report such indirect transfer to the relevant Chinese tax authority, which may in turn report upward to the SAT. Using general anti-tax avoidance provisions, the SAT may treat such indirect transfer as a direct transfer of Chinese interests if the transfer avoids Chinese tax by way of an arrangement without reasonable commercial purpose. As a result, gains derived from such indirect transfer may be subject to Chinese enterprise income tax, and the transferee or other person who is obligated to pay for the transfer would be obligated to withhold the applicable taxes, currently at a rate of up to 10% of the capital gain in the case of an indirect transfer of equity interests in a China resident enterprise. Both the transferor and the party obligated to withhold the applicable taxes may be subject to penalties under Chinese tax laws if the transferor fails to pay the taxes and the party obligated to withhold the applicable taxes fails to withhold the taxes.

The above regulations do not apply if either (i) the selling non-resident enterprise recognizes the relevant gain by purchasing and selling equity of the same listed enterprise in the open market (the “listed enterprise exception”); or (ii) the selling non-resident enterprise would have been exempted from enterprise income tax in China pursuant to applicable tax treaties or tax arrangements, if it had directly held and transferred such Chinese interests that were indirectly transferred. Under current law, the China indirect transfer rules do not apply to gains recognized by individual stockholders, regardless of whether or not they acquire or transfer our stock in open market transactions. However, in practice there have been a few reported cases of individuals being taxed on the indirect transfer of Chinese interests and the law could be changed so as to apply to individual stockholders, possibly with retroactive effect.

It is unclear whether Company stockholders that acquired Yum China stock through the distribution will be treated as acquiring Yum China stock in an open market purchase. If such acquisition of Yum China stock is not treated as acquired in an open market purchase, the listed transaction exception will not be available for transfers of such stock. We expect that transfers in open market transactions of our stock by corporate or other non-individual stockholders that have purchased our stock in open market transactions will not be taxable under the China indirect transfer rules due to the listed enterprise exception. Transfers, whether in the open market or otherwise, of our stock by corporate and other non-individual stockholders that acquired our stock in the distribution or in non-open market transactions may be taxable under the China indirect transfer rules and our China subsidiaries may have filing obligations in respect of such transfers upon the request of relevant China tax authorities. Transfers of our stock in non-open market transactions by corporate and other non-individual stockholders may be taxable under the China indirect transfer rules, whether or not such stock was acquired in open market transactions, and our China subsidiaries may have filing obligations in respect of such transfers upon the request of relevant China tax authorities. Corporate and other non-individual stockholders may be exempt from taxation under the China indirect transfer rules with respect to transfers of our stock if they are tax resident in a country or region that has a tax treaty or arrangement with China that provides for a capital gains tax exemption and they qualify for that exemption.

See Item 1A. “Risk Factors” for a discussion of risks relating to federal, state, local and international regulation relating to taxation of our business.

Employees

As of year-end 2016, the Company employed approximately 420,000 persons, approximately 90% of whom were restaurant team members who were employed on a full- or part-time basis with their pay calculated based on their service hours. The Company believes that it provides working conditions and compensation that compare favorably with those of our principal competitors. The majority of our employees are paid on an hourly basis. The Company considers our employee relations to be good.

Unconsolidated Affiliates

As of year-end 2016, 11% of our system wide restaurants were operated by unconsolidated affiliates that operated as franchisees. All of these restaurants were KFC restaurants, or 16% of total KFC restaurants as of year-end 2016. These unconsolidated affiliates are Chinese joint venture entities partially owned by the Company, which helped KFC establish its initial presence in certain regions of China.

Available Information

The Company makes available through the Investor Relations section of its internet website at <http://www.yumchina.com> its annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act, as soon as reasonably practicable after electronically filing such material with the U.S. Securities and Exchange Commission (“SEC”). These reports may also be obtained by visiting the SEC’s website at <http://www.sec.gov> or the SEC’s Public Reference Room at 100 F Street, NE, Washington, DC 20549 or by calling the SEC at 1 (800) SEC-0330.

Our Corporate Governance Principles and our Code of Conduct are also located within the Investor Relations section of the Company’s website at <http://www.yumchina.com>. The reference to the Company’s website address and the SEC’s website address is for informational purposes only, does not constitute incorporation by reference of the information contained on the websites and should not be considered part of this Form 10-K. These documents, as well as our SEC filings, are available in print free of charge to any stockholder who requests a copy from our Investor Relations Department by contacting Yum China at 7100 Corporate Drive, Plano, Texas 75024 United States of America, Attention: Investor Relations.

Executive Officers of the Registrant

The executive officers of the Company as of March 3, 2017, and their ages and current positions as of that date, are as follows:

Name	Age	Title
Muktesh “Micky” Pant	62	Chief Executive Officer
Edwin “Ted” Stedem	44	Chief Financial Officer
Joey Wat	45	President and Chief Operating Officer
Peter Kao	59	General Manager, Pizza Hut Casual Dining
Mark Chu	59	Senior Advisor to the Chief Executive Officer
Shella Ng	51	Chief Legal Officer and Corporate Secretary
Danny Tan	47	Chief Support Officer
Christabel Lo	54	Chief People Officer
Sunny Sun	44	Chief Growth Officer
Johnson Huang	54	General Manager, KFC
Ted Lee	50	General Manager, Little Sheep
Jeff Kuai	36	General Manager, Pizza Hut Home Service
Angela Ai	63	Chief Development Officer
Alice Wang	47	Senior Vice President, Public Affairs
Paul Hill	56	Vice President and Controller

Micky Pant has served as the Chief Executive Officer of Yum China and as a member of our board of directors since October 2016. He served as CEO of the YUM China Division (“Yum! Restaurants China”) from August 2015 to October 2016. Before becoming CEO of the Yum! Restaurants China, Mr. Pant has held a number of leadership positions at YUM, including CEO of the KFC Division, CEO of Yum! Restaurants International (“YRI”), President of Global Branding for YUM, President of YRI, Chief Marketing Officer of YUM, Global Chief Concept Officer for YUM and President of Taco Bell International. Before joining YUM, Mr. Pant built a foundation in marketing and international business with 15 years at Unilever in India and the U.K. and worked at PepsiCo, Inc. and Reebok International Limited. Since December 2014, Mr. Pant has served as an independent director on the board of Pinnacle Foods, Inc., where he also serves on the audit committee.

Ted Stedem has served as the Chief Financial Officer of Yum China since October 2016. He served as Chief Financial Officer of Yum! Restaurants China from August 2016 to October 2016. Prior to that position, Mr. Stedem served in a number of leadership roles for YUM since 2009, including General Manager and Managing Director of KFC Asia, Chief Financial Officer and Chief Development Officer of KFC South Pacific (SOPAC), and Vice President of Finance of Yum! Restaurants International. Prior to joining YUM, he worked in finance, business development and marketing roles with Merrill Lynch, Bain Consulting and Office Depot.

Joey Wat has served as the President and Chief Operating Officer of Yum China since February 2017. She served as Chief Executive Officer, KFC from October 2016 to February 2017, a position she held at Yum! Restaurants China from August 2015 to October 2016. Ms. Wat joined Yum! Restaurants China in September 2014 as President of KFC China and was promoted to Chief Executive Officer for KFC China in August 2015. Before joining YUM, Ms. Wat served in both management and strategy positions at AS Watson of Hutchinson Group (“Watson”), an international health, beauty and lifestyle retailer, in the U.K. from 2004 to 2014. Her last position at Watson was Managing Director of Watson U.K., which operates Superdrug and Savers, two retail chains specializing in the sale of pharmacy and health and beauty products, from 2012 to 2014. She made the transition from Head of Strategy of Watson in Europe to Managing Director of Savers in 2007. Before joining Watson, Ms. Wat spent seven years in management consulting including with McKinsey & Company’s Hong Kong office from 2000 to 2003.

Peter Kao has served as the General Manager, Pizza Hut Casual Dining since March 2017. He served as Chief Executive Officer, Pizza Hut Casual Dining from October 2016 to March 2017, a position he held at Yum! Restaurants China from August 2015 to October 2016. Mr. Kao previously served in the position of Senior Vice President & Brand General Manager of Pizza Hut for Yum! Restaurants China starting in 2013 and began leading both Pizza Hut Casual Dining and Pizza Hut Home Service as Brand General Manager in 2008. Mr. Kao has had several leadership positions at YUM, responsible for both Pizza Hut Casual Dining and Pizza Hut Home Service, since 2008. Before that, Mr. Kao served as Market Manager for the Eastern China Pizza Hut market since 1999. Prior to joining YUM in 1999, he held senior management roles in Club Development International, Sherwood Resort Guam, and Sherwood Hotel Taiwan.

Mark Chu has served as the Senior Advisor to the Chief Executive Officer of Yum China since October 2016. Mr. Chu is a long-term veteran of YUM and has held a number of leadership positions with Yum! Restaurants China, including President & Chief Development and Support Officer, President & Chief Operating Officer, Chief Development Officer, and Brand General Manager of KFC China. Mr. Chu joined YUM over two decades ago as Deputy General Manager of the Nanjing KFC market. Prior to joining YUM, Mr. Chu was the Area Supervisor of an international restaurant company in Taiwan.

Shella Ng has served as the Chief Legal Officer and Corporate Secretary of Yum China since October 2016. Ms. Ng joined YUM in 1995 and was appointed to Chief Legal Officer of Yum! Restaurants China in 2005. Prior to joining YUM, she worked for Freshfields Bruckhaus Deringer and Clifford Chance.

Danny Tan has served as the Chief Support Officer of Yum China since October 2016, a position he held at Yum! Restaurants China from January 2015 to October 2016. His responsibilities include overseeing food innovation, quality assurance, food safety, supply chain management, logistics and sourcing planning. Mr. Tan joined YUM in 1997 in the finance department of Yum! Restaurants China and began leading the logistics department in 2002. He subsequently led supply chain management as Senior Director from March 2014 to December 2014 before taking on his current role as Chief Support Officer. Prior to joining YUM, he was a Senior Analyst with Walt Disney, Hong Kong and a Senior Auditor with Deloitte & Touche, Singapore.

Christabel Lo has served as the Chief People Officer of Yum China since October 2016. Ms. Lo joined YUM in 1997 as the Training and Development Director of Yum! Restaurants China and was appointed to lead all of Human Resources in China in 2000, which she did until October 2016. Prior to joining YUM, Ms. Lo held a number of management positions in a variety of industries, including Managing Director of Dale Carnegie, Hong Kong, Head of International Personal Banking for Citibank, Hong Kong and Manager of Cheoy Lee Shipyards, Hong Kong.

Sunny Sun has served as the Chief Growth Officer of Yum China since October 2016, a position she held at Yum! Restaurants China from August 2016 to October 2016. Ms. Sun joined YUM in May 2015 as Vice President, Finance, Chief Strategist and Chief Financial Officer for Yum! Restaurants China, a position she held until July 2016. Prior to joining YUM, Ms. Sun was the Senior Managing Director of CVC Capital Partners, a private equity and investment advisory firm, from 2010 to 2014, and, before that, she was the Head of M&A Greater China for DaimlerChrysler from 2001 to 2010 and Senior Manager of Corporate Development with Danone Asia Pacific from 1998 to 2001.

Johnson Huang has served as General Manager, KFC since February 2017. He served as the Chief Information and Marketing Support Officer of the Company from October 2016 to February 2017, a position he held at Yum! Restaurants China from December 2014 to October 2016. Mr. Huang joined YUM in 2006 to lead the information technology department in China, and was named Chief Information Officer in 2013. He became our Chief Information and Marketing Support Officer in 2014 and assumed oversight of a spectrum of functions including IT, Digital, DSC, Marketing Shared Services and Engineering. He has been the key architect of Yum! Restaurants China's digital strategy and information technology roadmap in China. Prior to joining YUM, Mr. Huang held various information technology and business leadership positions with Cap Gemini Ernst & Young Group in Taiwan and the greater China region and Evergreen Group in Taiwan and the U.K.

Ted Lee has served as the General Manager, Little Sheep since March 2017. He served as Vice President and Brand General Manager, Little Sheep from October 2016 to March 2017, a position he held at Yum! Restaurants China from November 2014 to October 2016. Prior to joining YUM, Mr. Lee served as a director and Vice President & General Manager of Crocs China (Trade) Limited, a wholesale shoe manufacturer, from 2008 to 2014.

Jeff Kuai has served as the General Manager, Pizza Hut Home Service since March 2017. He served as Brand General Manager, Pizza Hut Home Service from October 2016 to March 2017, a position he held at Yum! Restaurants China from January 2015 to October 2016. From March 2012 to December 2014, Mr. Kuai was Director of Delivery Support Center of Yum! Restaurants China, where he was instrumental in building online ordering and e-commerce capabilities. Before that position, Mr. Kuai spent nine years in the information technology department of Yum! Restaurants China enhancing information technology infrastructure and productivity.

Angela Ai has served as the Chief Development Officer of Yum China since October 2016. Before her appointment to Chief Development Officer of Yum! Restaurants China in 2015, Ms. Ai was the Vice President, Development from 2008 to 2015, and served in management positions for KFC in Nanjing, Wuxi, Nanjing and Hangzhou from 1992 to 2008. Prior to joining YUM, she was the General Manager for China Merchant Group's department store and the Section Chief for Bureau of Youth League.

Alice Wang has served as the Senior Vice President, Public Affairs of Yum China since March 2017. She served as Vice President, Public Affairs from October 2016 to March 2017, a position she held at Yum! Restaurants China since she joined YUM in March 2015. Prior to joining YUM, Ms. Wang spent 22 years with Heinz China, a food products company, where she served as Vice President of Corporate Affairs, Greater China from August 2011 to February 2015.

Paul Hill has served as Vice President and Controller of Yum China since October 2016. He served as the Interim Chief Financial Officer of Yum! Restaurants China from June 2015 to January 2016. Before serving as Interim Chief Financial Officer, Mr. Hill was the Vice President, Division Controller of Yum! Restaurants China from 2012 to 2015, and, before that, he spent seven years as the Vice President, Division Controller for YRI. From 1995 to 2005, he held a variety of director and controller positions with YRI and PepsiCo. Prior to joining YUM, Mr. Hill spent 12 years as a Senior Manager in Audit and Consulting at KPMG.

Item 1A. Risk Factors.

You should carefully consider each of the following risks, as well as the information included elsewhere in this report, before deciding to invest in our common stock or otherwise in connection with evaluating our business. The risk factors have been separated into four general groups: risks related to our business and industry, risks related to doing business in China, risks related to the separation and related transactions and risks related to our common stock. Based on the information currently known to us, we believe that the following information identifies the most significant risk factors affecting us in each of these categories of risk. However, additional risks and uncertainties not presently known to us or that we currently believe to be immaterial may also adversely affect our business, financial condition or results of operations. In addition, past financial performance may not be a reliable indicator of future performance and historical trends should not be used to anticipate results or trends in future periods. If any of the following risks and uncertainties develops into actual events, these events could have a material adverse effect on our business, financial condition or results of operations. In such case, the trading price of our common stock could decline.

Risks Related to Our Business and Industry

Food safety and food-borne illness concerns may have an adverse effect on our reputation and business.

Food-borne illnesses, such as E. coli, hepatitis A, trichinosis and salmonella, occurred and may occur within our system from time to time. In addition, food safety issues such as food tampering, contamination and adulteration occur or may occur within our system from time to time. Any report or publicity linking us, our competitors, our restaurants, including restaurants operated by us or our franchisees, or any of YUM's restaurants, to instances of food-borne illness or food safety issues could adversely affect our restaurants' brands and reputations as well as our revenues and profits and possibly lead to product liability claims, litigation and damages. If a customer of our restaurants becomes ill from food-borne illnesses or as a result of food safety issues, restaurants in our system may be temporarily closed, which would decrease our revenues. In addition, instances or allegations of food-borne illness or food safety issues, real or perceived, involving our or YUM's restaurants, restaurants of competitors, or suppliers or distributors (regardless of whether we use or have used those suppliers or distributors), or otherwise involving the types of food served at our restaurants, could result in negative publicity that could adversely affect our sales. The occurrence of food-borne illnesses or food safety issues could also adversely affect the price and availability of affected ingredients, which could result in disruptions in our supply chain and/or lower margins for us and our franchisees.

Any failure to maintain effective quality control systems for our restaurants could have a material adverse effect on our business, reputation, results of operations and financial condition.

The quality and safety of the food we serve is critical to our success. Maintaining consistent food quality depends significantly on the effectiveness of our and our franchisees' quality control systems, which in turn depends on a number of factors, including the design of our quality control systems and employee implementation and compliance with those quality control policies and guidelines. Our quality control systems consist of (i) supplier quality control, (ii) logistics quality control, (iii) food processing plants' quality control, and (iv) restaurant quality control. There can be no assurance that our and our franchisees' quality control systems will prove to be effective. Any significant failure or deterioration of these quality control systems could have a material adverse effect on our business, reputation, results of operations and financial condition.

Any significant liability claims, food contamination complaints from our customers or reports of incidents of food tampering could adversely affect our business, reputation, results of operations and financial condition.

Being in the restaurant industry, we face an inherent risk of food contamination and liability claims. Our food quality depends partly on the quality of the food ingredients and raw materials provided by our suppliers, and we may not be able to detect all defects in our supplies. Any food contamination occurring in raw materials at our suppliers' food processing plants or during the transportation from food processing plants to our restaurants that we fail to detect or prevent could adversely affect the quality of the food served in our restaurants. Due to the scale of our and our franchisees' operations, we also face the risk that certain of our and our franchisees' employees may not adhere to our mandated quality procedures and requirements. Any failure to detect defective food supplies, or observe proper hygiene, cleanliness and other quality control requirements or standards in our operations could adversely affect the quality of the food we offer at our restaurants, which could lead to liability claims, complaints and related adverse publicity, reduced customer traffic at our restaurants, the imposition of penalties against us or our franchisees by relevant authorities and compensation awards by courts. Our sales have been significantly impacted by adverse publicity relating to supplier actions over the past decade. For example, our sales and perception of our brands were significantly impacted following adverse publicity relating to the failure of certain upstream poultry suppliers to meet our standards in late 2012 as well as adverse publicity relating to improper food handling practices by a separate, small upstream supplier in mid-2014. There can be no assurance that similar incidents will not occur again in the future or that we will not receive any food contamination claims or defective products from our suppliers in the future. Any such incidents could materially harm our business, reputation, results of operations and financial condition.

Health concerns arising from outbreaks of viruses or other diseases may have an adverse effect on our business.

Our business could be materially and adversely affected by the outbreak of a widespread health epidemic, such as avian flu, or H1N1, or "swine flu." The occurrence of such an outbreak of an epidemic illness or other adverse public health developments in China could materially disrupt our business and operations. Such events could also significantly impact our industry and cause a temporary closure of restaurants, which would severely disrupt our operations and have a material adverse effect on our business, results of operations and financial condition.

Our operations could be disrupted if any of our employees or employees of our business partners were suspected of having the swine flu or avian flu, since this could require us or our business partners to quarantine some or all of such employees or disinfect our restaurant facilities. Outbreaks of avian flu occur from time to time around the world, including in China where virtually all of our restaurants are located, and such outbreaks have resulted in confirmed human cases. It is possible that outbreaks in China and elsewhere could reach pandemic levels. Public concern over avian flu generally may cause fear about the consumption of chicken, eggs and other products derived from poultry, which could cause customers to consume less poultry and related products. This would likely result in lower revenues and profits. Avian flu outbreaks could also adversely affect the price and availability of poultry, which could negatively impact our profit margins and revenues.

Furthermore, other viruses may be transmitted through human contact, and the risk of contracting viruses could cause employees or guests to avoid gathering in public places, which could adversely affect restaurant guest traffic or the ability to adequately staff restaurants. We could also be adversely affected if jurisdictions in which we have restaurants impose mandatory closures, seek voluntary closures or impose restrictions on operations of restaurants. Even if such measures are not implemented and a virus or other disease does not spread significantly, the perceived risk of infection or health risk may affect our business.

We derive substantially all of our revenue from our operations in China.

Virtually all of our restaurants are located, and our revenues and profits originate, in China. As a consequence, our financial results are dependent on our results in China, and our business is highly exposed to all of the risks of doing business there. These risks are described further under the section “Risks Related to Doing Business in China.”

The operation of our restaurants is subject to the terms of the master license agreement.

Under the master license agreement with YUM, we are required to comply with certain brand standards established by YUM in connection with the licensed business. If our failure to comply with YUM’s standards of operations results in a material adverse effect on any of the brand businesses, YUM has various rights, including the right to terminate the applicable license or eliminate the exclusivity of our license in China.

Additionally, the master license agreement requires that we pay a license fee to YUM of 3% of gross revenue from Company and franchise restaurant sales, net of certain taxes and surcharges, of all restaurants of the licensed brands in China. Prior to the separation, we did not consider such license fee in the evaluation of which Company assets should be tested for impairment. Whether Company store-level assets are impaired will be determined by the overall business performance of the store at that time which will require an assessment of many operational factors. Nonetheless, it is possible that our impairment expense could increase going forward as a result of the inclusion of this license fee. While there may be other considerations that mitigate this expense, it is possible that the imposition of the license fee could impact our unit-level results, which could result in additional Company restaurant closures and/or lower new-unit development.

The master license agreement may be terminated upon the occurrence of certain events, such as the insolvency or bankruptcy of the Company. If the master license agreement were terminated, or any of our license rights were limited, our business, results of operations and financial condition would be adversely affected.

Our success is tied to the success of YUM’s brand strength, marketing campaigns and product innovation.

The KFC, Pizza Hut Casual Dining, Pizza Hut Home Service and Taco Bell trademarks and related intellectual property are owned by YUM and licensed to us in China, excluding Hong Kong, Taiwan and Macau. The value of these marks depends on the enforcement of YUM’s trademark and intellectual property rights, as well as the strength of YUM’s brands. Due to the nature of licensing and our agreements with YUM, our success is, to a large extent, directly related to the success of the YUM restaurant system, including the management, marketing success and product innovation of YUM. Further, if YUM were to reallocate resources away from the KFC, Pizza Hut Casual Dining, Pizza Hut Home Service or Taco Bell brands, these brands and the license rights that have been granted to us could be harmed globally or regionally, which could have a material adverse effect on our results of operations and our competitiveness in China. In addition, strategic decisions made by YUM management related to its brands, marketing and restaurant systems may not be in our best interests and may conflict with our strategic plans.

Shortages or interruptions in the availability and delivery of food and other supplies may increase costs or reduce revenues.

The products used in the operation of our restaurants are sourced from a wide variety of suppliers inside and outside of China. We are also dependent upon third parties to make frequent deliveries of food products and other supplies that meet our specifications at competitive prices. Shortages or interruptions in the supply of food products and other supplies to our restaurants could adversely affect the availability, quality and cost of items we use and the operations of our restaurants. Such shortages or disruptions could be caused by inclement weather, natural disasters such as floods, drought and hurricanes, increased demand, labor shortages, problems in production or distribution, restrictions on imports or exports, political instability in the countries in which suppliers and distributors are located, the financial instability of suppliers and distributors, suppliers' or distributors' failure to meet our standards, product quality issues, inflation, other factors relating to the suppliers and distributors and the countries in which they are located, food safety warnings or advisories or the prospect of such pronouncements or other conditions beyond our control. Despite our efforts in developing multiple suppliers for the same items, a shortage or interruption in the availability of certain food products or supplies could still increase costs and limit the availability of products critical to restaurant operations, which in turn could lead to restaurant closures and/or a decrease in sales. In addition, failure by a principal supplier or distributor for us and/or our franchisees to meet its service requirements could lead to a disruption of service or supply until a new supplier or distributor is engaged, and any disruption could have an adverse effect on our business.

In addition, we centrally purchase substantially all food and paper products, then sell and deliver them to most of our restaurants. We believe this central procurement model allows us to maintain quality control and achieve better prices and terms through volume purchases. However, we may not be able to accurately estimate the demand from franchisees and unconsolidated affiliates, which may result in excessive inventory. We may also not be able to timely collect payments from franchisees and unconsolidated affiliates, which could have a material adverse effect on our business, results of operations and financial condition.

We may not attain our target development goals; aggressive development could cannibalize existing sales; and new restaurants may not be profitable.

Our growth strategy depends on our ability to build new restaurants in China. The successful development of new units depends in large part on our ability to open new restaurants and to operate these restaurants profitably. We cannot guarantee that we, or our franchisees, will be able to achieve our expansion goals or that new restaurants will be operated profitably. Further, there is no assurance that any new restaurant will produce operating results similar to those of our existing restaurants. Other risks which could impact our ability to increase the number of our restaurants include prevailing economic conditions and our or our franchisees' ability to obtain suitable restaurant locations, negotiate acceptable lease or purchase terms for the locations, obtain required permits and approvals in a timely manner, hire and train qualified restaurant crews and meet construction schedules.

In addition, the new restaurants could impact the sales of our existing restaurants nearby. There can be no assurance that sales cannibalization will not occur or become more significant in the future as we increase our presence in existing markets in China.

Our growth strategy includes expanding our ownership and operation of restaurant units through organic growth by developing new restaurants that meet our investment objectives. We may not be able to achieve our growth objectives, and these new restaurants may not be profitable. The opening and success of restaurants we may open in the future depends on various factors, including:

- our ability to obtain or self-fund adequate development financing;
- competition from other QSRs in current and future markets;

- our degree of penetration in existing markets;
- the identification and availability of suitable and economically viable locations;
- sales and margin levels at existing restaurants;
- the negotiation of acceptable lease or purchase terms for new locations;
- regulatory compliance regarding restaurant opening and operation;
- the ability to meet construction schedules;
- our ability to hire and train qualified restaurant crews; and
- general economic and business conditions.

The prices of raw materials fluctuate.

Our restaurant business depends on reliable sources of large quantities of raw materials such as protein (including poultry, pork, beef and seafood), cheese, oil, flour and vegetables (including potatoes and lettuce). Our raw materials are subject to price volatility caused by any fluctuation in aggregate supply and demand, or other external conditions, such as climate and environmental conditions where weather conditions or natural events or disasters may affect expected harvests of such raw materials. As a result, the historical prices of raw materials consumed by us have fluctuated. We cannot assure you that we will continue to purchase raw materials at reasonable prices, or that our raw materials prices will remain stable in the future. In addition, because we and our franchisees provide competitively priced food, our ability to pass along commodity price increases to our customers is limited. If we are unable to manage the cost of our raw materials or to increase the prices of our products, it may have an adverse impact on our future profit margin.

We are subject to all of the risks associated with leasing real estate, and any adverse developments could harm our business, results of operations and financial condition.

As a significant number of our restaurants are operating on leased properties, we are exposed to the market conditions of the retail rental market. As of year-end 2016, we leased the land and/or building for approximately 6,008 restaurants in China. For information regarding our leased properties, please refer to Item 2. “Properties.” Accordingly, we are subject to all of the risks generally associated with leasing real estate, including changes in the investment climate for real estate, demographic trends, trade zone shifts, central business district relocations, and supply or demand for the use of the restaurants, as well as potential liability for environmental contamination.

We generally enter into lease agreements with initial terms of 10 to 20 years. Less than 5% of our existing leases expire before the end of 2017. Most of our lease agreements contain an early termination clause that permits us to terminate the lease agreement early if the restaurant’s unit contribution is negative for a specified period of time. We generally do not have renewal options for our leases and need to negotiate the terms of renewal with the lessor, who may insist on a significant modification to the terms and conditions of the lease agreement.

The rent under the majority of our current restaurant lease agreements is generally payable in one of three ways: (i) fixed rent; (ii) the higher of a fixed base rent or a percentage of the restaurant's annual sales revenue, subject to adjustment; or (iii) a percentage of the restaurant's annual sales revenue, subject to adjustment. Adjustments to rent calculated as a percentage of the restaurant's annual sales revenue generally correspond to the level of annual sales revenue as specified in the agreement. In addition to increases in rent resulting from fluctuations in annual sales revenue, certain of our lease agreements include provisions specifying fixed increases in rental payments over the respective terms of the lease agreements. While these provisions have been negotiated and are specified in the lease agreement, they will increase our costs of operation and therefore may materially and adversely affect our results of operation and financial condition if we are not able to pass on the increased costs to our customers. Certain of our lease agreements also provide for the payment of a management fee at either a fixed rate or fixed amount per square meter of the relevant leased property.

Where we do not have an option to renew a lease agreement, we must negotiate the terms of renewal with the lessor, who may insist on a significant modification to the terms and conditions of the lease agreement. If a lease agreement is renewed at a rate substantially higher than the existing rate, or if any existing favorable terms granted by the lessor are not extended, we must determine whether it is desirable to renew on such modified terms. If we are unable to renew leases for our restaurant sites on acceptable terms or at all, we will have to close or relocate the relevant restaurants, which would eliminate the sales that those restaurants would have contributed to our revenues during the period of closure, and could subject us to construction, renovation and other costs and risks. In addition, the revenue and any profit generated after relocation may be less than the revenue and profit previously generated before such relocation. As a result, any inability to obtain leases for desirable restaurant locations or renew existing leases on commercially reasonable terms could have a material adverse effect on our business, results of operations and financial condition.

We may not be able to obtain desirable restaurant locations on commercially reasonable terms.

We compete with other retailers and restaurants for suitable locations, and the market for retail premises is very competitive in China. Our competitors may negotiate more favorable lease terms than our lease terms, and some landlords and developers may offer priority or grant exclusivity to some of our competitors for desirable locations for various reasons beyond our control. We cannot provide assurance that we will be able to enter into new lease agreements for prime locations on commercially reasonable terms, if at all. If we cannot obtain desirable restaurant locations on commercially reasonable terms, our business, results of operations and ability to implement our growth strategy may be materially and adversely affected.

Labor shortages or increases in labor costs could slow our growth and harm our business and results of operations.

Restaurant operations are highly service-oriented, and our success depends in part upon our ability to attract, retain and motivate a sufficient number of qualified employees, including restaurant managers, and other crew members. The market for qualified employees in our industry is very competitive. Any future inability to recruit and retain qualified individuals may delay the planned openings of new restaurants and could adversely impact our existing restaurants. Any such delays, material increases in employee turnover rate in existing restaurants or widespread employee dissatisfaction could have a material adverse effect on our business and results of operations. In addition, competition for qualified employees could also compel us to pay higher wages to attract or retain key crew members, which could result in higher labor costs.

The Chinese Labor Contract Law that became effective on January 1, 2008 formalizes workers' rights concerning overtime hours, pensions, layoffs, employment contracts and the role of trade unions, and provides for specific standards and procedures for employees' protection. Moreover, minimum wage requirements in China have increased and could continue to increase our labor costs in the future. The salary level of employees in the restaurant industry in China has been increasing in the past several years. We may not be able to increase our product prices enough to pass these increased labor costs on to our customers, in which case our business and results of operations would be materially and adversely affected.

Our success depends substantially on our corporate reputation and on the value and perception of our brands.

One of our primary assets is the exclusive right to use the KFC, Pizza Hut Casual Dining, Pizza Hut Home Service and Taco Bell trademarks in restaurants in China. Our success depends in large part upon our ability and our franchisees' ability to maintain and enhance the value of these brands and our customers' loyalty to these brands in China. Brand value is based in part on consumer perceptions on a variety of subjective qualities. Business incidents, whether isolated or recurring, and whether originating from us, our franchisees, competitors, suppliers and distributors or YUM and its other licensees or franchisees, competitors, suppliers and distributors outside China can significantly reduce brand value and consumer trust, particularly if the incidents receive considerable publicity or result in litigation. For example, our brands could be damaged by claims or perceptions about the quality or safety of our products or the quality of our suppliers and distributors, regardless of whether such claims or perceptions are true. Any such incidents (even if resulting from the actions of a competitor) could cause a decline directly or indirectly in consumer confidence in, or the perception of, our brands and/or our products and reduce consumer demand for our products, which would likely result in lower revenues and profits. Additionally, our corporate reputation could suffer from a real or perceived failure of corporate governance or misconduct by a company officer, employee or representative.

Failure to protect the integrity and security of personal information of our customers and employees could result in substantial costs, expose us to litigation and damage our reputation.

We have been using, and plan to continue to use, digital technologies to improve the customer experience and drive sales growth. We, directly or indirectly, receive and maintain certain personal financial and other information about our customers when, for example, receiving online ordering, accepting cashless payments, conducting sales through online platforms and introducing brand loyalty programs.

If our security and information systems or the security and information systems of third-party service providers are compromised for any reason, including as a result of data corruption or loss, cyber-attack or a network security incident, or if our employees, franchisees or service providers fail to comply with laws, regulations and practice standards, and this information is obtained by unauthorized persons or used inappropriately, it could subject us to litigation and government enforcement actions, cause us to incur substantial costs, liabilities and penalties and/or result in a loss of customer confidence, any and all of which could adversely affect our business, reputation, results of operations and financial condition.

In addition, the use and handling of this information is regulated by evolving and increasingly demanding laws and regulations. The Chinese government recently promulgated a new cybersecurity law, to become effective on June 1, 2017, imposing tightened requirements on data privacy and cybersecurity practices. As such, we may be required to upgrade our current information technology infrastructure and systems and incur additional costs.

Our delivery business depends on the performance of, and our long-term relationships with, third-party aggregators and mobile payment processors.

Our delivery business represented approximately 10% of Company sales in 2016. KFC, Pizza Hut Casual Dining and Pizza Hut Home Service have partnered with third-party delivery aggregators, allowing our products to be listed on and ordered through their mobile or online platforms. For Pizza Hut Casual Dining, we also rely on the aggregators to deliver our products to customers. For KFC and Pizza Hut Home Service, we use outsourced riders to fulfill some of the delivery requirements. If we fail to extend or renew the agreements with these aggregators on acceptable terms, or at all, our business and results of operations may be materially adversely affected. In addition, these aggregators and outsourced riders may fail to follow the quality standards they agreed upon with us, in which case our business and reputation may suffer.

In 2016, mobile payments represented approximately 17% of company sales. In particular, the ability to accept mobile payments is critical to our delivery business. If mobile payment processors, such as Alipay and WeChat Pay, are unwilling or unable to provide us with payment processing service or impose onerous requirements on us in order to access their services, or if they increase the fees they charge us for these services, our business and results of operations could be harmed.

Our inability or failure to recognize, respond to and effectively manage the accelerated impact of social media could materially adversely impact our business and results of operations.

In recent years, there has been a marked increase in the use of social media platforms, including weblogs (blogs), mini-blogs, WeChat and other chat platforms, social media websites, and other forms of Internet-based communications, which allow individuals access to a broad audience of consumers and other interested persons. Many social media platforms immediately publish the content their subscribers and participants post, often without filters or checks on accuracy of the content posted. Information posted on such platforms at any time may be adverse to our interests and/or may be inaccurate. The online dissemination of negative comments about our brands and business, including inaccurate or irresponsible information, could harm our business, reputation, prospects, results of operations and financial condition. The damage may be immediate and intense, without affording us an opportunity for redress or correction, and we may not be able to recover from any negative publicity in a timely manner or at all.

Other risks associated with the use of social media include improper disclosure of proprietary information, exposure of personally identifiable information, fraud, hoaxes or malicious exposure of false information. The inappropriate use of social media by our customers or employees could increase our costs, lead to litigation or result in negative publicity that could damage our reputation and adversely affect our results of operations.

We could be party to litigation that could adversely affect us by increasing our expenses, diverting management attention or subjecting us to significant monetary damages and other remedies.

We are involved in legal proceedings from time to time. These proceedings do or could include consumer, employment, real-estate related, tort, intellectual property, breach of contract and other litigation. As a public company, we may in the future also be involved in legal proceedings alleging violation of securities laws or derivative litigation. Plaintiffs in these types of lawsuits often seek recovery of very large or indeterminate amounts, and the magnitude of the potential loss relating to such lawsuits may not be accurately estimated. Regardless of whether any claims against us are valid, or whether we are ultimately held liable, such litigation may be expensive to defend and may divert resources and management attention away from our operations and negatively impact reported earnings. With respect to insured claims, a judgment for monetary damages in excess of any insurance coverage could adversely affect our financial condition or results of operations. Any adverse publicity resulting from these allegations may also adversely affect our reputation, which in turn could adversely affect our results of operations.

In addition, the restaurant industry around the world has been subject to claims that relate to the nutritional content of food products, as well as claims that the menus and practices of restaurant chains have led to customer health issues, including weight gain and other adverse effects. We may also be subject to these types of claims in the future and, even if we are not, publicity about these matters (particularly directed at the quick service and fast-casual segments of the retail food industry) may harm our reputation and adversely affect our business, results of operations and financial condition.

Failure to comply with anti-bribery or anti-corruption laws could adversely affect our business and results of operations.

The U.S. Foreign Corrupt Practices Act and similar Chinese laws and other similar applicable laws prohibiting bribery of government officials and other corrupt practices are the subject of increasing emphasis and enforcement around the world. Although we continue to implement policies and procedures designed to duly comply with these laws, there can be no assurance that our employees, contractors, agents or other third parties will not take actions in violation of our policies or applicable law, particularly as we expand our operations through organic growth and acquisitions. Any such violations or suspected violations could subject us to civil or criminal penalties, including substantial fines and significant investigation costs, and could also materially damage the KFC, Pizza Hut Casual Dining, Pizza Hut Home Service and Taco Bell brands, as well as our reputation and prospects, business and results of operations. Publicity relating to any noncompliance or alleged noncompliance could also harm our reputation and adversely affect our business and results of operations.

As a U.S. company, we are subject to U.S. federal income tax on our worldwide income, which could result in material taxes in addition to the taxes on our China business.

Yum China is a Delaware corporation that indirectly owns the subsidiaries that conduct our business in China. As a Delaware corporation, we are subject to U.S. federal income tax on our worldwide income, including certain income that is distributed or deemed distributed to us by our subsidiaries operating in China. As a result, although substantially all of our profit is earned outside the U.S. and taxed at local tax rates that have historically been lower than the U.S. statutory tax rate, our after-tax income is determined based on U.S. tax rates, except with respect to any portion of our income that is permanently reinvested outside the U.S., thus reducing our after-tax profit.

In addition, as a holding company, our ability to make distributions (if any) to our stockholders generally is based on our ability to receive distributions from our subsidiaries. As a U.S. company, our receipt of any such distributions from our subsidiaries may result in the current recognition of U.S. taxable income and could cause our effective tax rate to increase to the extent such U.S. income taxes had not already been taken into account in such determination. This incremental U.S. tax cost could affect the amount of any distributions we are able to make to our stockholders.

Tax matters, including changes in tax rates, disagreements with taxing authorities and imposition of new taxes could impact our results of operations and financial condition.

We are subject to income taxes as well as non-income based taxes, such as value-added tax, customs duty, property tax, stamp duty, withholding taxes and obligations and local surcharges, in China and income tax and other taxes in the U.S. and other jurisdictions. We are also subject to reviews, examinations and audits by Chinese tax authorities, the U.S. Internal Revenue Service (the "IRS"), and other taxing authorities with respect to income and non-income based taxes. If Chinese tax authorities, the IRS, or another taxing authority disagrees with our tax positions, we could face additional tax liabilities, including interest and penalties. Payment of such additional amounts upon final settlement or adjudication of any disputes could have a material impact on our results of operations and financial condition.

In addition, we are directly and indirectly affected by new tax legislation and regulation and the interpretation of tax laws and regulations worldwide. Recently, the new U.S. presidential administration has made public statements indicating that it has made international tax reform a priority, and key members of the U.S. Congress have conducted hearings and proposed new legislation. Certain changes to U.S. tax laws currently proposed by lawmakers would impact the ability of U.S. taxpayers to defer U.S. taxation of foreign earnings and to claim and utilize foreign tax credits. These proposals would also eliminate certain tax deductions until earnings are repatriated to the United States. We cannot predict the impact, if any, of these changes to our business.

Moreover, the tax regime in China is rapidly evolving and there can be significant uncertainty for taxpayers in China as Chinese tax laws may change significantly or be subject to uncertain interpretations. Since 2012, the Chinese government launched a VAT pilot reform to replace BT (“VAT pilot program”) to make reform to its retail tax structure by ending the co-existence of BT and VAT where BT would be gradually phased out and replaced by VAT. The retail tax structure reform is intended to be a progressive and positive shift to more closely align with a more modern service-based economy. Effective May 1, 2016, the retail tax structure reform has been rolled out to cover all business sectors nationwide where the BT has been completely replaced by VAT. The VAT reform is still at an early stage of implementation, and the interpretation and application of the new VAT regime may not be immediately clear or settled at some local governmental levels. In addition, the timetable for enacting the prevailing VAT regulations into national VAT law, including ultimate enacted VAT rates, is not clear. Changes in legislation, regulation or interpretation of existing laws and regulations in the U.S., China, and other jurisdictions where we are subject to taxation could increase our taxes and have an adverse effect on our results of operations and financial condition.

Our results of operations may be adversely impacted by changes in consumer discretionary spending and general economic conditions.

Purchases at our restaurants are discretionary for consumers and, therefore, our results of operations are susceptible to economic slowdowns and recessions. Our results of operations are dependent upon discretionary spending by consumers, which may be affected by general economic conditions in China. Some of the factors that impact discretionary consumer spending include unemployment rates, fluctuations in the level of disposable income, the price of gasoline, stock market performance and changes in the level of consumer confidence. These and other macroeconomic factors could have an adverse effect on our sales, profitability or development plans, which could harm our results of operations and financial condition.

The retail food industry in which we operate is highly competitive.

The retail food industry in which we operate is highly competitive with respect to price and quality of food products, new product development, advertising levels and promotional initiatives, customer service, reputation, restaurant location, and attractiveness and maintenance of properties. If consumer or dietary preferences change, or our restaurants are unable to compete successfully with other retail food outlets in new and existing markets, our business could be adversely affected. We also face growing competition as a result of convergence in grocery, convenience, deli and restaurant services, including the offering by the grocery industry of convenient meals, including pizzas and entrees with side dishes. Competition from delivery aggregators and other food delivery services in China has also increased in recent years, particularly in urbanized areas. Increased competition could have an adverse effect on our sales, profitability or development plans, which could harm our results of operations and financial condition.

Any inability to successfully compete with the other restaurants and catering services in our markets may prevent us from increasing or sustaining our revenues and profitability and could have a material adverse effect on our business, results of operations, financial condition and/or cash flows. We may also need to modify or refine elements of our restaurant system in order to compete with popular new restaurant styles or concepts, including delivery aggregators, that develop from time to time. There can be no assurance that we will be successful in implementing any such modifications or that such modifications will not reduce our profitability.

We require various approvals, licenses and permits to operate our business and the loss of or failure to obtain or renew any or all of these approvals, licenses and permits could adversely affect our business and results of operations.

In accordance with the laws and regulations of China, we are required to maintain various approvals, licenses and permits in order to operate our restaurant business. Each of our restaurants in China is required to obtain the relevant food hygiene license or food service license, public assembly venue hygiene license, environmental protection assessment and inspection approval and fire safety design approval and fire prevention inspection report, and some of our restaurants which sell alcoholic beverages are required to make further registrations or obtain additional approvals. These licenses and registrations are achieved upon satisfactory compliance with, among other things, the applicable food safety, hygiene, environmental protection, fire safety and alcohol laws and regulations. Most of these licenses are subject to periodic examinations or verifications by relevant authorities and are valid only for a fixed period of time and subject to renewal and accreditation. There is no assurance that we or our franchisees will be able to obtain or maintain any of these licenses.

We may not be able to adequately protect the intellectual property we own or have the right to use, which could harm the value of our brands and adversely affect our business and operations.

We believe that our brands are essential to our success and our competitive position. Although the trademarks we use in China are duly registered, these steps may not be adequate to protect these intellectual property rights. In addition, third parties may infringe upon the intellectual property rights we own or have the right to use or misappropriate the proprietary knowledge we use in our business, primarily our proprietary recipes, which could have a material adverse effect on our business, results of operations or financial condition. The laws of China may not offer the same protection for intellectual property rights as the U.S. and other jurisdictions with more robust intellectual property laws.

We are required under the master license agreement with YUM to police, protect and enforce the trademarks and other intellectual property rights used by us, and to protect trade secrets. Such actions to police, protect or enforce could result in substantial costs and diversion of resources, which could negatively affect our sales, profitability and prospects. Furthermore, the application of laws governing intellectual property rights in China is uncertain and evolving, and could involve substantial risks to us. Even if actions to police, protect or enforce are resolved in our favor, we may not be able to successfully enforce the judgment and remedies awarded by the court and such remedies may not be adequate to compensate us for our actual or anticipated losses.

In addition, we may face claims of infringement that could interfere with the use of the proprietary know-how, concepts, recipes or trade secrets we use in our business. Defending against such claims may be costly and, if we are unsuccessful, we may be prohibited from continuing to use such proprietary information in the future or be forced to pay damages, royalties or other fees for using such proprietary information, any of which could negatively affect our sales, profitability and prospects.

Our licensor may not be able to adequately protect its intellectual property, which could harm the value of the KFC, Pizza Hut Casual Dining, Pizza Hut Home Service and Taco Bell brands and branded products and adversely affect our business, results of operations and financial condition.

The success of our business depends in large part on our continued ability to use the trademarks, service marks, recipes and other components of the KFC, Pizza Hut Casual Dining, Pizza Hut Home Service and Taco Bell branded systems that we license from YUM pursuant to the master license agreement we entered into in connection with the separation.

We are not aware of any assertions that the trademarks, menu offerings or other intellectual property rights we license from YUM infringe upon the proprietary rights of third parties, but third parties may claim infringement by us or YUM in the future. Any such claim, whether or not it has merit, could be time-consuming, result in costly litigation, cause delays in introducing new menu items in the future or require us to enter into additional royalty or licensing agreements with third parties. As a result, any such claims could have a material adverse effect on our business, results of operations and financial condition.

Our results of operations may fluctuate due to seasonality and certain major events in China.

Our sales are subject to seasonality. For example, we typically experience higher sales during traditional Chinese festivals and holiday seasons and lower sales and lower operating profit during the second and fourth quarters. As a result of these fluctuations, softer sales during a period in which we have historically experienced higher sales could have a disproportionately negative effect on our full-year results, and comparisons of sales and results of operations within a financial year may not be able to be relied on as indicators of our future performance. Any seasonal fluctuations reported in the future may differ from the expectations of our investors.

Our information systems may fail or be damaged, which could harm our operations and our business.

Our operations are dependent upon the successful and uninterrupted functioning of our computer and information systems. Our systems could be exposed to damage or interruption from fire, natural disaster, power loss, telecommunications failure, unauthorized entry and computer viruses. System defects, failures, interruptions, unauthorized entries or viruses could result in:

- additional computer and information security and systems development costs;
- diversion of technical and other resources;
- loss of customers and sales;
- loss or theft of customer, employee or other data;
- negative publicity;
- harm to our business and reputation; and
- exposure to litigation claims, government investigations and enforcement actions, fraud losses or other liabilities.

To the extent we rely on the systems of third parties in areas such as credit card processing, telecommunications and wireless networks, any defects, failures and interruptions in such systems could result in similar adverse effects on our business. Sustained or repeated system defects, failures or interruptions could materially impact our operations and results of operations. Also, if we are unsuccessful in updating, upgrading and expanding our systems, our ability to increase comparable store sales, improve operations, implement cost controls and grow our business may be constrained.

Despite the implementation of security measures, our infrastructure may be vulnerable to physical break-ins, computer viruses, programming errors, attacks by third parties or similar disruptive problems.

We may be unable to detect, deter and prevent all instances of fraud or other misconduct committed by our employees, customers or other third parties.

As we operate in the restaurant industry, we usually receive and handle relatively large amounts of cash in our daily operations. Instances of fraud, theft or other misconduct with respect to cash can be difficult to detect, deter and prevent, and could subject us to financial losses and harm our reputation.

We may be unable to prevent, detect or deter all such instances of misconduct. Any such misconduct committed against our interests, which may include past acts that have gone undetected or future acts, may have a material adverse effect on our business and results of operations.

Changes in accounting standards and subjective assumptions, estimates and judgments by management related to complex accounting matters could significantly affect our results of operations and financial condition.

Generally accepted accounting principles and related accounting pronouncements, implementation guidelines and interpretations with regard to a wide range of matters that are relevant to our business, including revenue recognition, long-lived asset impairment, impairment of goodwill and other intangible assets, and share-based compensation, are highly complex and involve many subjective assumptions, estimates and judgments. Changes in these rules or their interpretation or changes in underlying assumptions, estimates or judgments could significantly change our reported or expected financial performance or financial condition. New accounting guidance may require systems and other changes that could increase our operating costs and/or change our financial statements. For example, implementing future accounting guidance related to leases and other areas impacted by the convergence project between the Financial Accounting Standards Board and the International Accounting Standards Board could require us to make significant changes to our lease management system or other accounting systems, and will result in changes to our financial statements.

Our insurance policies may not provide adequate coverage for all claims associated with our business operations.

We have obtained insurance policies that we believe are customary and appropriate for businesses of our size and type and at least in line with the standard commercial practice in China. However, there are types of losses we may incur that cannot be insured against or that we believe are not cost effective to insure, such as loss of reputation. If we were held liable for uninsured losses or amounts or claims for insured losses exceeding the limits of our insurance coverage, our business and results of operations may be materially and adversely affected.

Failure by us to maintain effective disclosure controls and procedures and internal control over financial reporting in accordance with the rules of the SEC could harm our business and results of operations and/or result in a loss of investor confidence in our financial reports, which could have a material adverse effect on our business.

We are required to maintain effective disclosure controls and procedures and effective internal control over financial reporting in connection with our filing of periodic reports with the SEC under the Exchange Act. Failure to maintain effective disclosure controls and procedures and internal control over financial reporting or to comply with Section 404 of the Sarbanes-Oxley Act of 2002, or any report by us of a material weakness in such controls, may cause investors to lose confidence in our financial statements. If we fail to remedy any material weakness, our financial statements may be inaccurate and we may face restricted access to the capital markets, which could adversely affect our business, results of operations and financial condition.

Unforeseeable business interruptions could adversely affect our business.

Our operations are vulnerable to interruption by fires, floods, earthquakes, power failures and power shortages, hardware and software failures, computer viruses and other events beyond our control. In particular, our business is dependent on prompt delivery and reliable transportation of our food products by our logistics partners. Unforeseeable events, such as adverse weather conditions, natural disasters, severe traffic accidents and delays, non-cooperation of our logistics partners, and labor strikes, could lead to delay or lost deliveries to our restaurants, which may result in the loss of revenue or in customer claims. There may also be instances where the conditions of fresh, chilled or frozen food products, being perishable goods, deteriorate due to delivery delays, malfunctioning of refrigeration facilities or poor handling during transportation by our logistics partners. This may result in a failure by us to provide quality food and services to customers, thereby affecting our business and potentially damaging our reputation. Any such events experienced by us could disrupt our operations.

Risks Related to Doing Business in China

Changes in Chinese political policies and economic and social policies or conditions may materially and adversely affect our business, results of operations and financial condition and may result in our inability to sustain our growth and expansion strategies.

Substantially all of our assets and business operations are located in China. Accordingly, our business, results of operations, financial condition and prospects may be influenced to a significant degree by political, economic and social conditions in China generally, by continued economic growth in China as a whole, and by geopolitical stability in the region. For example, our results of operations in the third quarter of 2016 were adversely impacted by an international court ruling in July 2016 regarding claims to sovereignty over the South China Sea, which triggered a series of regional protests and boycotts in China, intensified by social media, against a few international companies with well-known Western brands.

The Chinese economy, markets and levels of consumer spending are influenced by many factors beyond our control, including current and future economic conditions, political uncertainty, unemployment rates, inflation, fluctuations in the level of disposable income, taxation, foreign exchange control, and changes in interest and currency exchange rates. The Chinese economy differs from the economies of most developed countries in many respects, including the level of government involvement, level of development, growth rate, foreign exchange control and fiscal measures and allocation of resources. Although the Chinese government has implemented measures since the late 1970s emphasizing the utilization of market forces for economic reform, the restructuring of state assets and state owned enterprises, and the establishment of improved corporate governance in business enterprises, a significant portion of productive assets in China is still owned or controlled by the Chinese government. The Chinese government also exercises significant control or influence over Chinese economic growth through allocating resources, controlling payment of foreign currency-denominated obligations, setting monetary and fiscal policies, regulating financial services and institutions and providing preferential treatment to particular industries or companies.

While the Chinese economy has experienced significant growth in recent decades, growth has been uneven, both geographically and among various sectors of the economy. The Chinese government has implemented various measures to encourage economic growth and guide the allocation of resources. Some of these measures benefit the overall Chinese economy but may also have a negative effect on us. Our results of operations and financial condition could be materially and adversely affected by government control over capital investments or changes in tax regulations that are applicable to us. In addition, the Chinese government has implemented certain measures, including interest rate increases, to control the pace of economic growth. These measures may cause decreased economic activity in China. Since 2012, Chinese economic growth has slowed and any prolonged slowdown in the Chinese economy may reduce the demand for our products and adversely affect our business, results of operations and financial condition. Restaurant dining, and specifically casual dining, is discretionary for customers and tends to be higher during periods in which favorable economic conditions prevail. Customers' tendency to become more cost-conscious as a result of an economic slowdown or decreases in disposable income may reduce our customer traffic or average revenue per customer, which may adversely affect our revenues.

Uncertainties with respect to the interpretation and enforcement of Chinese laws, rules and regulations could have a material adverse effect on us.

Substantially all of our operations are conducted in China, and are governed by Chinese laws, rules and regulations. Our subsidiaries are subject to laws, rules and regulations applicable to foreign investment in China. The Chinese legal system is a civil law system based on written statutes. Unlike common law systems, it is a system in which legal cases may be cited for reference but have limited value as precedents. In the late 1970s, the Chinese government began to promulgate a comprehensive system of laws and regulations governing economic matters in general. The overall effect of legislation over the past four decades has significantly increased the protections afforded to various forms of foreign or private-sector investment in China. However, since these laws and regulations are relatively new and the Chinese legal system continues to rapidly evolve, the interpretations of many laws, regulations and rules are not always uniform and enforcement of these laws, regulations and rules involve uncertainties.

From time to time, we may have to resort to administrative and court proceedings to interpret and/or enforce our legal rights. However, since Chinese administrative and court authorities have significant discretion in interpreting and implementing statutory and contractual terms, it may be more difficult to evaluate the outcome of administrative and court proceedings, and the level of legal protection we enjoy, than in more developed legal systems. Any administrative and court proceedings in China may be protracted, resulting in substantial costs and diversion of resources and management attention. Furthermore, the Chinese legal system is based in part on government policies and internal rules (some of which are not published in a timely manner or at all) that may have retroactive effect.

As a result, we may not be aware of our violation of these policies and rules until sometime after the violation. Such uncertainties, including uncertainty over the scope and effect of our contractual, property (including intellectual property) and procedural rights, and any failure to respond to changes in the regulatory environment in China could materially adversely affect our business and impede our ability to continue our operations.

Fluctuation in the value of the RMB may have a material adverse effect on your investment.

The conversion of Chinese Renminbi (“RMB”) into foreign currencies, including U.S. dollars, is based on rates set by the People’s Bank of China (“PBOC”). The Chinese government allowed the RMB to appreciate by more than 20% against the U.S. dollar between July 2005 and July 2008. Between July 2008 and June 2010, the exchange rate between the RMB and the U.S. dollar remained within a narrow range. After June 2010, the Chinese government allowed the RMB to appreciate slowly against the U.S. dollar again. On August 11, 2015, however, the PBOC allowed the RMB to depreciate by approximately 2% against the U.S. dollar. In 2016, the RMB further fell more than 6% against U.S. dollar, representing the biggest yearly depreciation of the RMB since 1994. Changes in the value of the RMB against the U.S. dollar may occur relatively suddenly, as was the case, for example, in August 2015. It is difficult to predict how market forces or Chinese or U.S. government policy may impact the exchange rate between the RMB and the U.S. dollar in the future.

Substantially all of our revenues and costs are denominated in RMB. As a Delaware holding company, we may rely on dividends and other fees paid to us by our subsidiaries in China. Any significant revaluation of the RMB may materially affect our cash flows, net revenues, earnings and financial position, and the value of, and any dividends payable on, our common stock in U.S. dollars. For example, an appreciation of the RMB against the U.S. dollar would make any new RMB-denominated investments or expenditures more costly to us, to the extent that we need to convert U.S. dollars into RMB for such purposes. Conversely, a significant depreciation of the RMB against the U.S. dollar may significantly reduce the U.S. dollar equivalent of our earnings, which in turn could adversely affect the price of our common stock. If we decide to convert RMB into U.S. dollars for the purpose of making payments for dividends on our common stock, strategic acquisitions or investments or other business purposes, appreciation of the U.S. dollar against the RMB would have a negative effect on the U.S. dollar amount available to us.

Very few hedging options are available in China to reduce our exposure to exchange rate fluctuations. In addition, our currency exchange loss may be magnified by Chinese exchange control regulations that restrict our ability to convert RMB into foreign currency. As a result, fluctuations in exchange rates and restrictions on exchange may have a material adverse effect on your investment.

Governmental control of currency conversion and payments of foreign currency and RMB out of mainland China may limit our ability to utilize our cash balances effectively and affect the value of your investment.

The Chinese government imposes controls on the convertibility of the RMB into foreign currencies and, in certain cases, the remittance of both foreign currency and RMB out of mainland China. Under our current corporate structure as a Delaware holding company, our income is primarily derived from the earnings from our Chinese subsidiaries. Substantially all revenues of our Chinese subsidiaries are denominated in RMB. Shortages in the availability of foreign currency and control on payments out of mainland China may restrict the ability of our Chinese subsidiaries to remit sufficient foreign currency and/or RMB to pay dividends or to make other payments to us, or otherwise to satisfy their obligations. Under existing Chinese foreign exchange regulations, payments of current account items, including profit distributions, license fee payments and expenditures from trade-related transactions, can be made in foreign currencies or RMB without prior approval from China's State Administration of Foreign Exchange ("SAFE") and PBOC by complying with certain procedural requirements. However, for any Chinese company, dividends can be declared and paid only out of the retained earnings of that company under Chinese law. Furthermore, approval from SAFE or its local branch may be required where RMB are to be converted into foreign currencies, and approval from SAFE and PBOC or their branches may be required where foreign currency and/or RMB are to be remitted out of mainland China. Specifically, under the existing restrictions, without a prior approval of SAFE and PBOC, cash generated from the operations of our subsidiaries in China may not be used to pay dividends to Yum China, pay the license fee to YUM, pay employees who are located outside mainland China, pay off debt owed by our subsidiaries to entities outside mainland China, or make capital expenditures outside mainland China.

The Chinese government may also at its discretion restrict access in the future to foreign currencies or further restrict payments of foreign currency and RMB out of mainland China. If the foreign exchange control system prevents us from obtaining sufficient foreign currency to satisfy our currency demands or restricts us from paying the license fee to YUM, we may not be able to pay dividends to our stockholders, fulfill our license fee payment obligation, pay out service fees to vendors and repay our indebtedness when due. There can be no assurance that the rules and regulations pursuant to which SAFE and PBOC grant or deny approvals will not change in a way that adversely affects the ability of our Chinese subsidiaries to repatriate funds out of mainland China or pay license fees. Any such limitation could materially and adversely affect our ability to pay dividends or otherwise fund and conduct our business.

Changes in the laws and regulations of China or non-compliance with applicable laws and regulations may have a significant impact on our business, results of operations and financial condition.

Our business and operations are subject to the laws and regulations of China. The continuance of our operations depends upon compliance with, *inter alia*, applicable Chinese environmental, health, safety, labor, social security, pension and other laws and regulations. Failure to comply with such laws and regulations could result in fines, penalties or lawsuits. In addition, there is no assurance that we will be able to comply fully with applicable laws and regulations should there be any amendment to the existing regulatory regime or implementation of any new laws and regulations.

Furthermore, our business and operations in China entail the procurement of licenses and permits from the relevant authorities. Difficulties or failure in obtaining the required permits, licenses and certificates could result in our inability to continue our business in China in a manner consistent with past practice. In such an event, our business, results of operations and financial condition may be adversely affected.

We rely to a significant extent on dividends and other distributions on equity paid by our principal operating subsidiaries in China to fund offshore cash requirements.

We are a holding company and conduct all of our business through our operating subsidiaries. We rely to a significant extent on dividends and other distributions on equity paid by our principal operating subsidiaries for our cash requirements. As noted above, distributions to us from our subsidiaries may result in incremental tax costs.

The laws, rules and regulations applicable to our Chinese subsidiaries permit payments of dividends only out of their accumulated profits, if any, determined in accordance with applicable Chinese accounting standards and regulations. In addition, under Chinese law, an enterprise incorporated in China is required to set aside at least 10% of its after-tax profits each year, after making up previous years' accumulated losses, if any, to fund certain statutory reserve funds, until the aggregate amount of such a fund reaches 50% of its registered capital. As a result, our Chinese subsidiaries are restricted in their ability to transfer a portion of their net assets to us in the form of dividends. At the discretion of the board of directors, as an enterprise incorporated in China, each of our Chinese subsidiaries may allocate a portion of its after-tax profits based on Chinese accounting standards to staff welfare and bonus funds. These reserve funds and staff welfare and bonus funds are not distributable as cash dividends. Any limitation on the ability of our Chinese subsidiaries to pay dividends or make other distributions to us could limit our ability to make investments or acquisitions outside of China that could be beneficial to our business, pay dividends, or otherwise fund and conduct our business.

In addition, the EIT Law and its implementation rules provide that a withholding tax at a rate of 10% will be applicable to dividends payable by Chinese companies to companies that are not China resident enterprises unless otherwise reduced according to treaties or arrangements between the Chinese central government and the governments of other countries or regions where the non-China resident enterprises are incorporated. Although a foreign tax credit is generally available against our U.S. federal income taxes for such withholding taxes, the ability to utilize foreign tax credits is subject to complex limitations and as such we may be limited in our ability to offset any such Chinese withholding tax against our U.S. federal income tax liabilities.

Restrictive covenants in bank credit facilities, joint venture agreements or other arrangements that we or our subsidiaries may enter into in the future may also restrict the ability of our subsidiaries to pay dividends or make distributions or remittances to us. These restrictions could reduce the amount of dividends or other distributions we receive from our subsidiaries, which in turn could restrict our ability to return capital to our stockholders in the future.

Under the EIT Law, if we are classified as a China resident enterprise for Chinese enterprise income tax purposes, such classification would likely result in unfavorable tax consequences to us and our non-Chinese stockholders.

Under the EIT Law and its implementation rules, an enterprise established outside China with a “de facto management body” within China is considered a China resident enterprise for Chinese enterprise income tax purposes. A China resident enterprise is generally subject to certain Chinese tax reporting obligations and a uniform 25% enterprise income tax rate on its worldwide income. Furthermore, under the EIT Law, if we are a China resident enterprise (i) dividends paid by us to our non-Chinese stockholders would be subject to a 10% dividend withholding tax or a 20% individual income tax if the stockholder is an individual and (ii) such non-Chinese stockholders may become subject to Chinese tax and filing obligations as well as withholding with respect to any disposition of our stock, subject to certain treaty or other exemptions or reductions.

We and each of our subsidiaries that is organized outside of China intend to conduct our and their management functions in a manner that does not cause us or them to be China resident enterprises, including by carrying on day-to-day management activities and maintaining key records, such as resolutions of the board of directors and resolutions of stockholders, outside of China. As such, we do not believe that we or any of our non-Chinese subsidiaries should be considered a China resident enterprise for purposes of the EIT Law. However, given the uncertainty regarding the application of the EIT Law to us and our future operations, there can be no assurance that we or any of our non-Chinese subsidiaries will not be treated as a China resident enterprise now or in the future for Chinese tax law purposes.

We and our stockholders face uncertainty with respect to indirect transfers of equity interests in China resident enterprises through transfer of non-Chinese-holding companies. Enhanced scrutiny by the Chinese tax authorities may have a negative impact on potential acquisitions and dispositions we may pursue in the future.

In February 2015, the SAT issued Bulletin 7, pursuant to which an “indirect transfer” of Chinese interests by a non-resident enterprise may be recharacterized and treated as a direct transfer of Chinese taxable assets, if such arrangement does not have reasonable commercial purpose and the transferor avoids payment of Chinese enterprise income tax. Where a non-resident enterprise conducts an “indirect transfer” of Chinese interests by disposing of equity interests in an offshore holding company that directly or indirectly owns Chinese interests, the transferor, transferee and/or the China resident enterprise may report such indirect transfer to the relevant Chinese tax authority, which may in turn report upward to the SAT. Using general anti-tax avoidance provisions, the SAT may treat such indirect transfer as a direct transfer of Chinese interests if the transfer avoids Chinese tax by way of an arrangement without reasonable commercial purpose. As a result, gains derived from such indirect transfer may be subject to Chinese enterprise income tax, and the transferee or other person who is obligated to pay for the transfer would be obligated to withhold the applicable taxes, currently at a rate of up to 10% of the capital gain in the case of an indirect transfer of equity interests in a China resident enterprise. Both the transferor and the party obligated to withhold the applicable taxes may be subject to penalties under Chinese tax laws if the transferor fails to pay the taxes and the party obligated to withhold the applicable taxes fails to withhold the taxes. However, the above regulations do not apply if either (i) the selling non-resident enterprise recognizes the relevant gain by purchasing and selling equity of the same listed enterprise in the open market (the “listed enterprise exception”); or (ii) the selling non-resident enterprise would have been exempted from enterprise income tax in China pursuant to applicable tax treaties or tax arrangements, if it had directly held and transferred such Chinese interests that were indirectly transferred. Under current law, the China indirect transfer rules do not apply to gains recognized by individual stockholders, regardless of whether or not they acquire or transfer our stock in open market transactions. However, in practice there have been a few reported cases of individuals being taxed on the indirect transfer of Chinese interests and the law could be changed so as to apply to individual stockholders, possibly with retroactive effect.

It is unclear whether stockholders that acquired our stock through the distribution will be treated as acquiring such stock in an open market purchase. If such stock is not treated as acquired in an open market purchase, the listed transaction exception will not be available for transfers of such stock. We expect that transfers in open market transactions of our stock by corporate or other non-individual stockholders that have purchased our stock in open market transactions will not be taxable under the China indirect transfer rules due to the listed enterprise exception. Transfers, whether in the open market or otherwise, of our stock by corporate and other non-individual stockholders that acquired our stock in the distribution or in non-open market transactions may be taxable under the China indirect transfer rules and our China subsidiaries may have filing obligations in respect of such transfers, upon the request of relevant China tax authorities. Transfers of our stock in non-open market transactions by corporate and other non-individual stockholders may be taxable under the China indirect transfer rules, whether or not such stock was acquired in open market transactions, and our China subsidiaries may have filing obligations in respect of such transfers upon the request of relevant China tax authorities. Corporate and other non-individual stockholders may be exempt from taxation under the China indirect transfer rules with respect to transfers of our stock if they are tax resident in a country or region that has a tax treaty or arrangement with China that provides for a capital gains tax exemption and they qualify for that exemption.

In addition, we may be subject to these indirect transfer rules in the event of any future sale of a China resident enterprise through the sale of a non-Chinese holding company, or the purchase of a China resident enterprise through the purchase of a non-Chinese holding company. Our company and other non-resident enterprises in our group may be subject to filing obligations or taxation if our company and other non-resident enterprises in our group are transferors in such transactions, and may be subject to withholding obligations if our company and other non-resident enterprises in our group are transferees in such transactions.

You may experience difficulties in effecting service of legal process, enforcing foreign judgments or bringing original actions in China based on United States or other foreign laws against us and our management.

We conduct substantially all of our operations in China and substantially all of our assets are located in China. In addition, some of our directors and executive officers reside within China. As a result, it may not be possible to effect service of process within the United States or elsewhere outside of China upon these persons, including with respect to matters arising under applicable U.S. federal and state securities laws. It may also be difficult for investors to bring an original lawsuit against us or our directors or executive officers based on U.S. federal securities laws in a Chinese court. Moreover, China does not have treaties with the United States providing for the reciprocal recognition and enforcement of judgments of courts. Therefore, even if a judgment were obtained against us or our management for matters arising under U.S. federal or state securities laws or other applicable U.S. federal or state law, it may be difficult to enforce such a judgment.

Certain defects caused by non-registration of our lease agreements related to certain properties occupied by us in China may materially and adversely affect our ability to use such properties.

As of December 31, 2016, we leased approximately 6,008 properties in China, and to our knowledge, the lessors of most properties leased by us, most of which are used as premises for our restaurants, had not registered the lease agreements with government authorities in China.

According to Chinese laws, a lease agreement is generally required to be registered with the relevant land and real estate administration bureau. However, the enforcement of this legal requirement varies depending on the local regulations and practices and, in cities where we operate a significant number of restaurants, the local land and real estate administration bureaus no longer require registration or no longer impose fines for failure to register the lease agreements. In addition, our standard lease agreements require the lessors to make such registration and, although we have proactively requested that the applicable lessors complete or cooperate with us to complete the registration in a timely manner, we are unable to control whether and when such lessors will do so.

A failure to register a lease agreement will not invalidate the lease agreement but may subject the parties to a fine. Depending on the local regulations, the lessor alone or both the lessor and lessee are under the obligation to register a lease agreement with the relevant land and real estate administration bureau. In the event that a fine is imposed on both the lessor and lessee, and if we are unable to recover from the lessor any fine paid by us based on the terms of the lease agreement, such fine will be borne by us.

To date, the operation of our restaurants has not been disrupted due to the non-registration of our lease agreements. No fines, actions or claims have been instituted against us or, to our knowledge, the lessors with respect to the non-registration of our lease agreements. However, we cannot assure you that our lease agreements relating to, and our right to use and occupy, our premises will not be challenged in the future.

Our restaurants are susceptible to risks in relation to unexpected land acquisitions, building closures or demolitions.

The Chinese government has the statutory power to acquire any land use rights of land plots and the buildings thereon in China in the public interest subject to certain legal procedures. Under the Regulations for the Expropriation of and Compensation for Housing on State-owned Land, issued by the State Council, which became effective as of January 21, 2011, there is no legal provision that the tenant of an expropriated property is entitled to compensation. Generally speaking, only the owner of such property is entitled to compensation from the government. The claims of the tenant against the landlord will be subject to the terms of the lease agreement. In the event of any compulsory acquisition, closure or demolition of any of the properties at which our restaurants or facilities are situated, we may not receive any compensation from the government or the landlord. In such event, we may be forced to close the affected restaurant(s) or relocate to other locations, which may have an adverse effect on our business and results of operations.

Any failure to comply with Chinese regulations regarding our employee equity incentive plans may subject Chinese plan participants or us to fines and other legal or administrative sanctions.

Pursuant to SAFE Circular 37, China residents who participate in share incentive plans in overseas non-publicly listed companies may submit applications to SAFE or its local branches for foreign exchange registration with respect to offshore special purpose companies. We and our directors, executive officers and other employees who are Chinese citizens or who have resided in China for a continuous period of not less than one year and who have been granted restricted shares, restricted stock units (“RSUs”), stock appreciation rights (“SARs”), or options are subject to the Notice on Issues Concerning the Foreign Exchange Administration for Domestic Individuals Participating in Stock Incentive Plan of Overseas Publicly Listed Company, issued by SAFE in February 2012, according to which, employees, directors, supervisors and other management members participating in any stock incentive plan of an overseas publicly-listed company who are Chinese citizens or who are non-Chinese citizens residing in China for a continuous period of not less than one year, subject to limited exceptions, are required to register with SAFE through a domestic qualified agent, which could be a Chinese subsidiary of such overseas listed company, and complete certain other procedures. Failure to complete SAFE registrations may result in fines and legal sanctions and may also limit our ability to make payments under our equity incentive plans or receive dividends or sales proceeds related thereto, or our ability to contribute additional capital into our wholly-foreign owned enterprises in China and limit our wholly-foreign owned enterprises’ ability to distribute dividends to us. We also face regulatory uncertainties that could restrict our ability to adopt additional equity incentive plans for our directors and employees under Chinese law.

In addition, the SAT has issued circulars concerning employee SARs, share options and restricted shares. Under these circulars, employees working in China who exercise share options, or whose restricted shares or RSUs vest, will be subject to Chinese individual income tax. The Chinese subsidiaries of an overseas listed company have obligations to file documents related to employee share options or restricted shares with relevant tax authorities and to withhold individual income taxes of those employees related to their share options, restricted shares, SARs or RSUs. Although we currently intend to withhold income tax from our Chinese employees in connection with their exercise of options and SARs and the vesting of their restricted shares and RSUs, if the employees fail to pay, or our Chinese subsidiaries fail to withhold, their income taxes according to relevant laws, rules and regulations, our Chinese subsidiaries may face sanctions imposed by the tax authorities or other Chinese government authorities.

Failure to make adequate contributions to various employee benefit plans as required by Chinese regulations may subject us to penalties.

Companies operating in China are required to participate in various government-sponsored employee benefit plans, including certain social insurance, housing funds and other welfare-oriented payment obligations, and contribute to the plans in amounts equal to certain percentages of salaries, including bonuses and allowances, of their employees up to a maximum amount specified by the local government from time to time at locations where they operate their businesses. While we believe we comply with all material aspects of relevant regulations, the requirements governing employee benefit plans have not been implemented consistently by the local governments in China given the different levels of economic development in different locations. If we are subject to late fees or fines in relation to the underpaid employee benefits, our results of operations and financial condition may be adversely affected.

The audit report included in this annual report on Form 10-K is prepared by auditors who are not currently inspected by the Public Company Accounting Oversight Board and, as such, our stockholders are deprived of the benefits of such inspection.

As an auditor of companies that are publicly traded in the United States and a firm registered with the Public Company Accounting Oversight Board (“PCAOB”), our independent registered public accounting firm is required under the laws of the United States to undergo regular inspections by the PCAOB. However, because we have substantial operations within China, our independent registered public accounting firm’s audit documentation related to their audit report included in this annual report on Form 10-K is located in China. The PCAOB is currently unable to conduct full inspections in China or review audit documentation located within China without the approval of Chinese authorities.

Inspections of other auditors conducted by the PCAOB outside of China have at times identified deficiencies in those auditors’ audit procedures and quality control procedures, which may be addressed as part of the inspection process to improve future audit quality. The lack of PCAOB inspections of audit work undertaken in China prevents the PCAOB from regularly evaluating our auditor’s audits and its quality control procedures. As a result, stockholders may be deprived of the benefits of PCAOB inspections, and may lose confidence in our reported financial information and procedures and the quality of our financial statements.

Proceedings instituted by the SEC against certain China-based accounting firms, including our independent registered public accounting firm, could result in our financial statements being determined to not be in compliance with the requirements of the Exchange Act.

In late 2012, the SEC commenced administrative proceedings under Rule 102(e) of its Rules of Practice and also under the Sarbanes-Oxley Act of 2002 against the Chinese member firms of the “big four” accounting firms, including our independent registered public accounting firm. The Rule 102(e) proceedings initiated by the SEC relate to the failure of these firms to produce certain documents, including audit work papers, in response to a request from the SEC pursuant to Section 106 of the Sarbanes-Oxley Act of 2002. The auditors located in China claim they are not in a position lawfully to produce such documents directly to the SEC because of restrictions under Chinese law and specific directives issued by the China Securities Regulatory Commission (“CSRC”). The issues raised by the proceedings are not specific to our auditor or to us, but potentially affect equally all PCAOB-registered audit firms based in China and all businesses based in China (or with substantial operations in China) with securities listed in the United States. In addition, auditors based outside of China are subject to similar restrictions under Chinese law and CSRC directives in respect of audit work that is carried out in China which supports the audit opinions issued on financial statements of entities with substantial China operations.

In January 2014, the administrative judge reached an initial decision that the Chinese member firms of the “big four” accounting firms should be barred from practicing before the SEC for a period of six months. In February 2014, the accounting firms filed a petition for review of the initial decision. In February 2015, the Chinese member firms of the “big four” accounting firms reached a settlement with the SEC. As part of the settlement, each of the “big four” accounting firms agreed to a censure and to pay a fine to the SEC to settle the dispute with the SEC. The settlement stays the current proceeding for four years, during which time the firms are required to follow detailed procedures to seek to provide the SEC with access to Chinese firms’ audit documents via the CSRC. If a firm does not follow the procedures, the SEC may impose penalties such as suspensions, or commence a new, expedited administrative proceeding against any non-compliant firm. The SEC could also restart administrative proceedings against all four firms.

If our independent registered public accounting firm were denied, even temporarily, the ability to practice before the SEC, and we are unable to timely find another independent registered public accounting firm to audit and issue an opinion on our financial statements, our financial statements could be determined not to be in compliance with the requirements of the Exchange Act. Such a determination could ultimately lead to delisting of our common stock from the New York Stock Exchange. Moreover, any negative news about the proceedings against these audit firms may adversely affect investor confidence in companies with substantial China based operations listed on securities exchanges in the United States. All of these factors could materially and adversely affect the market price of our common stock and our ability to access the capital markets.

Chinese regulation of loans to, and direct investment in, Chinese entities by offshore holding companies and governmental control of currency conversion may restrict or prevent us from making loans or additional capital contributions to our Chinese subsidiaries, which may materially and adversely affect our liquidity and our ability to fund and expand our business.

We are a Delaware holding company conducting our operations in China through our Chinese subsidiaries. We may make loans to our Chinese subsidiaries, or we may make additional capital contributions to our Chinese subsidiaries, or we may establish new Chinese subsidiaries and make capital contributions to these new Chinese subsidiaries, or we may acquire offshore entities with business operations in China in an offshore transaction.

Most of these uses are subject to Chinese regulations and approvals. For example, loans by us to our wholly-owned Chinese subsidiaries to finance their activities cannot exceed statutory limits and must be registered with the local counterpart of SAFE. If we decide to finance our wholly-owned Chinese subsidiaries by means of capital contributions, in practice, we might be still required to obtain approval from the China Ministry of Commerce (“MOFCOM”) or its local counterpart.

On August 29, 2008, SAFE promulgated the Circular on the Relevant Operating Issues Concerning the Improvement of the Administration of the Payment and Settlement of Foreign Currency Capital of Foreign-Invested Enterprises, or SAFE Circular 142, regulating the conversion by a foreign-invested enterprise of foreign currency registered capital into RMB by restricting how the converted RMB may be used. SAFE Circular 142 provides that RMB capital converted from foreign currency registered capital of a foreign-invested enterprise may only be used for purposes within the business scope approved by the applicable governmental authority and may not be used for equity investments within China with limited exceptions (*e.g.*, by holding companies, venture capital or private equity firms). In addition, SAFE strengthened its oversight of the flow and use of the RMB capital converted from the foreign currency registered capital of a foreign-invested company. The use of such RMB capital may not be altered without SAFE approval, and such RMB capital may not in any case be used to repay RMB loans if the proceeds of such loans have not been used. Such requirements are also known as the “payment-based foreign currency settlement system” established under SAFE Circular 142. Violations of SAFE Circular 142 could result in monetary or other penalties. Furthermore, SAFE promulgated a circular on November 9, 2010, known as Circular 59, and another supplemental circular on July 18, 2011, known as Circular 88, which both tightened the examination of the authenticity of settlement of foreign currency capital or net proceeds from overseas listings. SAFE further promulgated the Circular on Further Clarification and Regulation of the Issues Concerning the Administration of Certain Capital Account Foreign Exchange Businesses, or Circular 45, on November 9, 2011, which expressly prohibited foreign-invested enterprises from using registered capital settled in RMB converted from foreign currencies to grant loans through entrustment arrangements with a bank, repay inter-company loans or repay bank loans that have been transferred to a third party. Circular 142, Circular 59, Circular 88 and Circular 45 may significantly limit our ability to make loans or capital contributions to our Chinese subsidiaries and to convert such proceeds into RMB, which may adversely affect our liquidity and our ability to fund and expand our business in China.

Furthermore, on April 8, 2015, SAFE promulgated the Circular on the Reform of the Administrative Method of the Settlement of Foreign Currency Capital of Foreign-Invested Enterprises, or Circular 19, which became effective as of June 1, 2015. This Circular 19 is to implement the so-called “conversion-at-will” of foreign currency in capital account, which was established under a circular issued by SAFE on August 4, 2014, or Circular 36, and was implemented in 16 designated industrial parks as a reform pilot. The Circular 19 now implements the conversion-at-will of foreign currency settlement system nationally, and it abolishes the application of Circular 59 and Circular 45 on March 19, 2015 as well as Circular 142, Circular 88 and Circular 36 starting from June 1, 2015. Among other things, under Circular 19, foreign-invested enterprises may either continue to follow the payment-based foreign currency settlement system or elect to follow the conversion-at-will of foreign currency settlement system. Where a foreign-invested enterprise follows the conversion-at-will of foreign currency settlement system, it may convert any or 100% of the amount of the foreign currency in its capital account into RMB at any time. The converted RMB will be kept in a designated account known as “Settled but Pending Payment Account,” and if the foreign-invested enterprise needs to make further payment from such designated account, it still needs to provide supporting documents and go through the review process with its bank. If under special circumstances the foreign-invested enterprise cannot provide supporting documents in time, Circular 19 grants the banks the power to provide a grace period to the enterprise and make the payment before receiving the supporting documents. The foreign-invested enterprise will then need to submit the supporting documents within 20 working days after payment. In addition, foreign-invested enterprises are now allowed to use their converted RMB to make equity investments in China under Circular 19. However, foreign-invested enterprises are still required to use the converted RMB in the designated account within their approved business scope under the principle of authenticity and self-use. It remains unclear whether a common foreign-invested enterprise, other than such special types of enterprises as holding companies, venture capital or private equity firms, can use the converted RMB in the designated account to make equity investments if equity investment or similar activities are not within their approved business scope.

In light of the various requirements imposed by Chinese regulations on loans to and direct investment in Chinese entities by offshore holding companies as discussed above, we cannot assure you that we will be able to complete the necessary government registrations or obtain the necessary government approvals on a timely basis, or at all, with respect to future loans by us to our Chinese subsidiaries or with respect to future capital contributions by us to our Chinese subsidiaries. If we fail to complete such registrations or obtain such approvals, our ability to capitalize or otherwise fund our Chinese operations may be negatively affected, which could materially and adversely affect our liquidity and our ability to fund and expand our business.

Risks Related to the Separation and Related Transactions

The separation may not achieve some or all of the anticipated benefits.

We may not realize some or all of the anticipated strategic, financial, operational or other benefits from the separation. The separation and distribution is expected to provide the following benefits, among others:

- allowing our company to focus on and more effectively pursue our own distinct operating priorities and strategies, and enabling our management to concentrate efforts on the unique needs of our business and pursue distinct opportunities for long-term growth and profitability;
- permitting our company to concentrate our financial resources solely on our own operations, providing greater flexibility to invest capital in our business in a time and manner appropriate for our distinct strategy and business needs and facilitating a more efficient allocation of capital;
- creating an independent equity structure that will afford our company direct access to capital markets and facilitating our ability to capitalize on our unique growth opportunities and effect future acquisitions utilizing our common stock;

- facilitating incentive compensation arrangements for employees more directly tied to the performance of our business, and enhancing employee hiring and retention by, among other things, improving the alignment of management and employee incentives with performance and growth objectives; and
- allowing investors to separately value our company based on our unique investment identity, including the merits, performance and future prospects of our business, and providing investors with a distinct and targeted investment opportunity.

We may not achieve these and other anticipated benefits for a variety of reasons, including, among others:

- operating as an independent publicly traded company requires a significant amount of management's time and effort, which may divert management's attention from operating and growing our business;
- we may be more susceptible to market fluctuations and other adverse events as a result of the separation than if we were still a part of YUM; and
- our business is less diversified than YUM's business prior to the separation.

If the distribution does not qualify as a transaction that is generally tax-free for U.S. federal income tax purposes, the Company could be subject to significant tax liabilities, and, in certain circumstances, the Company could be required to indemnify YUM for material taxes and other related amounts pursuant to indemnification obligations under the tax matters agreement.

The distribution was conditioned on YUM's receipt of opinions of outside advisors regarding the tax-free treatment of the distribution for U.S. federal income tax purposes. The opinions relied on various assumptions and representations as to factual matters made by YUM and us which, if inaccurate or incomplete in any material respect, would jeopardize the conclusions reached by such advisors in their opinions. The opinions are not binding on the IRS or the courts, and there can be no assurance that the IRS or the courts will not challenge the conclusions stated in the opinions or that any such challenge would not prevail.

If, notwithstanding receipt of the opinions, the distribution were determined to be a taxable transaction, YUM would be treated as having sold shares of the Company in a taxable transaction, likely resulting in a significant taxable gain. Pursuant to the tax matters agreement, the Company and YCCL agreed to indemnify YUM for any taxes and related losses resulting from any breach of covenants regarding the preservation of the tax-free status of the distribution, certain acquisitions of our equity securities or assets, or those of certain of our affiliates or subsidiaries, and any breach by us or any member of our group of certain representations in the documents delivered by us in connection with the distribution. Therefore, if the distribution fails to qualify as a transaction that is generally tax-free as a result of one of these actions or events, we may be required to make material payments to YUM under this indemnity.

YUM may be subject to Chinese indirect transfer tax with respect to the distribution, in which event we could be required to indemnify YUM for material taxes and related amounts pursuant to indemnification obligations under the tax matters agreement.

As noted above, Bulletin 7 provides that in certain circumstances a non-resident enterprise may be subject to Chinese enterprise income tax on an "indirect transfer" of Chinese interests. YUM concluded, and we concurred, that it believes that the distribution had a reasonable commercial purpose and that it is more likely than not that YUM will not be subject to this tax with respect to the distribution. However, there are uncertainties regarding the circumstances in which the tax will apply, and there can be no assurances that the Chinese tax authorities will not seek to impose this tax on YUM.

Pursuant to the tax matters agreement, the Company and YCCL have agreed to indemnify YUM for a portion (tied to the relative market capitalization of YUM and the Company during the thirty trading days after the distribution) of any taxes and related losses resulting from the application of Bulletin 7 to the distribution. Alternatively, if Bulletin 7 applies to the distribution as a result of a breach by the Company or Company group members of certain representations or covenants, or due to certain actions of the Company or Company group members following the distribution, the Company and YCCL generally will indemnify YUM for all such taxes and related losses. Therefore, if YUM is subject to such Chinese tax with respect to the distribution, we may be required to make material payments to YUM under this indemnity. Such payments could have a material adverse effect on our financial condition.

As a result of the separation, our ability to engage in strategic transactions may be limited. In addition, we could be liable for adverse tax consequences resulting from engaging in such transactions.

To preserve the tax-free treatment to YUM and its shareholders of the separation and the distribution for U.S. federal income tax purposes, under the tax matters agreement that we entered into with YUM, for a period of time following the distribution, we generally will be prohibited from taking certain actions that could prevent the distribution and related transactions from qualifying as a transaction that is generally tax-free, for U.S. federal income tax purposes under Sections 355 and 361 of the U.S. Internal Revenue Code (the “Code”). Under the tax matters agreement, for the two-year period following the distribution, the Company will be prohibited, except in certain circumstances, from:

- facilitating, permitting, or participating in any transaction or transactions resulting in the acquisition of 40% or more of its stock;
- entering into any transaction or transactions resulting in the acquisition of 50% or more of its assets, whether by merger or otherwise;
- transferring assets in certain tax-free mergers or consolidations or liquidating;
- issuing equity securities other than pursuant to certain employment related issuances;
- redeeming or repurchasing its capital stock other than in certain open market transactions; and
- ceasing to actively conduct its business.

In addition, the Company is prohibited from taking any action that, or failing to take any action the failure of which to take, would be inconsistent with the tax-free treatment of the distribution and related transactions.

These restrictions may limit our ability to pursue certain strategic transactions or other transactions that may maximize the value of our business.

The distribution may be taxable to YUM and the Company if there is an acquisition of 50% or more of YUM or Company common stock.

Even if the distribution otherwise qualifies as a transaction that is generally tax-free for U.S. federal income tax purposes, the distribution of Company common stock to YUM shareholders in connection with the distribution would result in significant U.S. federal income tax liabilities to YUM under the Code (but not to YUM shareholders) if it were deemed part of a “plan” pursuant to which one or more persons acquire, directly or indirectly, shares representing a 50% or greater interest (by vote or value) in YUM or the Company.

For purposes of determining whether the distribution of Company common stock to YUM shareholders in connection with the distribution is disqualified as tax-free to YUM under the rules described in the preceding paragraph, any acquisitions of the stock of YUM or the Company within two years before or after the distribution may be presumed to be part of such a “plan,” although the parties may be able to rebut that presumption. For purposes of this test, acquisitions of Company common stock by Pollos Investment L.P., an affiliate of Primavera Capital Group (“Primavera”), and API (Hong Kong) Investment Limited, an affiliate of Zhejiang Ant Small and Micro Financial Services Group Co., Ltd. (“Ant Financial” and together with Primavera, the “Investors”), within two years after the distribution will likely be treated as part of such a “plan.” In particular, under the terms of the investment agreements among the Company, YUM and the Investors, the Investors acquired in the aggregate 4.8% of the Company’s issued and outstanding common stock, which acquisition will be taken into account for purposes of this test. Also, under the terms of the shareholders agreement entered into with the Investors, the Investors are permitted to acquire more Company common stock in the two years following the distribution (including pursuant to the warrants held by the Investors), provided that the Investors’ shares of Company common stock (in the aggregate) do not exceed 19.9% of the total shares of the Company’s outstanding common stock (subject to certain conditions in the shareholders agreement). Any such additional acquisitions of Company common stock by the Investors in the two years following the distribution will similarly be taken into account for purposes of this test. If one or more other persons acquire, directly or indirectly, shares of the Company that, together with such acquisitions by the Investors in the two years after the distribution, represent a 50% or greater interest (by vote or value) in the Company, such acquisitions may be deemed part of a “plan” that includes the distribution.

The rules for determining whether shares representing a 50% or greater interest (by vote or value) in YUM or the Company have been acquired as part of a “plan” that includes the distribution are complex, inherently factual and subject to interpretation of the facts and circumstances of a particular case. If the Company does not carefully monitor its compliance with these rules, it might inadvertently cause or permit such a prohibited change in the ownership of its stock to occur, resulting in significant federal income tax liabilities to YUM under the Internal Revenue Code. Under the terms of the tax matters agreement among YUM, YCCL and the Company entered into in connection with the distribution, YCCL and the Company are generally required to indemnify YUM against any such tax liabilities, which may have a material adverse effect on the Company. These indemnity obligations could also discourage or prevent a third party from making a proposal to acquire the Company during the relevant period.

We have limited history operating as an independent publicly traded company and our accounting and other management systems and resources may not be adequately prepared to meet the financial reporting and other requirements to which we are subject.

Prior to the separation and distribution, our financial results were included within the consolidated results of YUM, and our reporting and control systems were appropriate for those of a subsidiary of a public company. We have only recently been directly subject to reporting and other requirements of the Exchange Act, and Section 404 of the Sarbanes-Oxley Act of 2002. As an independent company, we are subject to additional reporting and other requirements, which require, among other things, annual management assessments of the effectiveness of our internal controls over financial reporting and a report by our independent registered public accounting firm addressing these assessments. Section 404 of the Sarbanes-Oxley Act of 2002 requires that we include a report from management on the effectiveness of our internal control over financial reporting in our annual report beginning with our annual report for the fiscal year ending December 31, 2017. In addition, beginning at the same time, our independent registered public accounting firm must report on the effectiveness of our internal control over financial reporting. These and other obligations may place significant demands on our management, administrative and operational resources, including accounting and IT resources.

To comply with these requirements, we may need to implement additional financial and management controls, reporting systems and procedures and hire additional staff. We expect to incur additional annual expenses related to these steps, which expenses may be significant. If we are unable to upgrade our financial and management controls, reporting systems and procedures in a timely and effective fashion, our ability to comply with our financial reporting requirements and other rules that apply to reporting companies could be impaired. Any failure to achieve and maintain effective internal controls could have a material adverse effect on our business, results of operations and financial condition.

Being a public company subject to additional laws, rules and regulations requires the investment of additional resources to comply with these laws, rules and regulations. In this regard, we have incurred and will continue to incur expenses related to, among other things, director and officer liability insurance, director fees, expenses associated with our SEC reporting obligations, transfer agent fees, increased auditing and legal fees and similar expenses, which expenses may be significant.

Our management has limited experience managing a public company, and regulatory compliance may divert management's attention from the day-to-day management of our business.

Our management team has limited experience managing a publicly traded company, interacting with public company investors or complying with the increasingly complex laws and requirements pertaining to public companies. These requirements include record keeping, financial reporting and corporate governance rules and regulations and involve significant regulatory oversight and reporting obligations under U.S. federal securities laws and the scrutiny of securities analysts and investors. These new obligations require substantial attention from our management team and could divert its attention away from the day-to-day management of our business, which could adversely affect our business, results of operations and financial condition.

There can be no assurance that we will have access to the capital markets on terms acceptable to us.

From time to time, we may need to access the long-term and short-term capital markets to obtain financing. Although we believe that our existing sources of capital will permit us to finance our operations for the foreseeable future on acceptable terms and conditions, our access to, and the availability of, financing on acceptable terms and conditions in the future or at all will be impacted by many factors, including, but not limited to:

- our financial performance;
- our credit ratings or absence of a credit rating;
- the liquidity of the overall capital markets; and
- the state of the Chinese, U.S. and global economies.

There can be no assurance, particularly as a relatively new company that currently has no credit rating, that we will have access to the capital markets on terms acceptable to us or at all.

We have incurred and will continue to incur increased administrative and other costs by virtue of our status as an independent public company. Our historical financial information for periods prior to the distribution is not necessarily representative of the results that we would have achieved as a separate, publicly traded company and may not be a reliable indicator of our future results.

Our historical information for periods prior to the distribution refers to our business as operated by and integrated with YUM. Such information is derived from or based on the consolidated financial statements and accounting records of YUM. Accordingly, our historical financial information for periods prior to the distribution does not necessarily reflect the financial condition, results of operations or cash flows that we would have achieved as a separate, publicly traded company during the periods presented or those that we will achieve in the future primarily as a result of the following factors, among others:

- Prior to the separation, our business was operated by YUM as part of its broader corporate organization, rather than as an independent company. YUM or one of its affiliates performed various corporate functions for us such as legal, treasury, accounting, internal auditing, human resources and public affairs. Our historical financial results for periods prior to the distribution reflect allocations of corporate expenses from YUM for such functions which are likely to be less than the expenses we would have incurred had we operated as a separate publicly traded company. As a result of the separation, our costs related to such functions previously performed by YUM may increase.
- Historically, we shared with YUM economies of scope and scale in costs, employees and vendor relationships. Although we entered into certain agreements with YUM in connection with the separation, these arrangements may not fully capture the benefits that we enjoyed as a result of being integrated with YUM and may result in us paying higher charges than in the past for these services. These circumstances could have an adverse effect on our results of operations and financial condition.
- Generally, our working capital requirements and capital for our general corporate purposes, including acquisitions and capital expenditures, had historically been satisfied as part of the corporate-wide cash management policies of YUM. As an independent company, we may need to obtain additional financing from banks, through public offerings or private placements of debt or equity securities, through strategic relationships or from other arrangements, which may or may not be available and may be more costly.
- As a result of the separation, the cost of capital for our business may be higher than YUM's cost of capital prior to the separation.

Other significant changes may occur in our cost structure, management, financing and business operations as a result of operating as a company separate from YUM.

The master license agreement that we entered into with YUM limits our ability to compete with YUM and contains other restrictions on our operations.

The master license agreement includes non-compete provisions pursuant to which we generally agree to not compete with YUM. The master license agreement also contains other restrictions on our operations, including restrictions on us or our affiliates from engaging in a "competing business" in China and other countries in which YUM operates its brands during the term of the agreement and for twelve months following the expiration, termination or transfer of the agreement or an interest in the agreement.

These restrictions could materially and adversely affect our business, results of operations and financial condition.

YUM may fail to perform under certain transaction agreements that we entered into with it as part of the separation, and we may not have necessary systems and services in place when these transaction agreements expire.

In connection with the separation, the Company and YUM entered into several agreements, including among others a master license agreement, a separation and distribution agreement, a tax matters agreement, an employee matters agreement, a transition services agreement and a name license agreement. The master license agreement establishes a bilateral relationship between YUM and us for an initial term of fifty (50) years subject to renewal as described in Item 1. “Business – Trademarks and Patents.” The separation and distribution agreement, tax matters agreement, employee matters agreement, transition services agreement and name license agreement determine, among other things, the allocation of assets and liabilities between the companies and include any necessary indemnifications related to liabilities and obligations. If YUM is unable to satisfy its obligations under these agreements, we could incur operational difficulties or losses that could have a material and adverse effect on our business, results of operations and financial condition.

Potential indemnification liabilities owing to YUM pursuant to the separation and distribution agreement could materially and adversely affect our business, results of operations and financial condition.

The separation and distribution agreement provides for, among other things, indemnification obligations generally designed to make us financially responsible for (i) certain liabilities associated with our business; (ii) our failure to pay, perform or otherwise promptly discharge any liabilities or contracts relating to the Company business, in accordance with their respective terms, whether prior to, at or after the distribution; (iii) any guarantee, indemnification obligation, surety bond or other credit support agreement, arrangement, commitment or understanding by YUM for our benefit, unless related to liabilities primarily associated with the YUM business; (iv) certain tax liabilities; (v) any breach by us of the separation and distribution agreement or any of the ancillary agreements or any action by us in contravention of our amended and restated certificate of incorporation or amended and restated bylaws; and (vi) any untrue statement or alleged untrue statement of a material fact or omission or alleged omission to state a material fact required to be stated therein or necessary to make the statements therein not misleading, with respect to all information contained in the information statement relating to the distribution or any other disclosure document that describes the separation or the distribution or the Company and its subsidiaries or primarily relates to the transactions contemplated by the separation and distribution agreement, subject to certain exceptions. If we are required to indemnify YUM under the circumstances set forth in the separation and distribution agreement, we may be subject to substantial liabilities.

In connection with the separation, YUM has agreed to indemnify us for certain liabilities. However, there can be no assurance that the indemnity will be sufficient to insure us against the full amount of such liabilities, or that YUM’s ability to satisfy its indemnification obligation will not be impaired in the future.

Pursuant to the separation and distribution agreement and certain other agreements we entered into with YUM, YUM has agreed to indemnify us for certain liabilities set forth in the separation and distribution agreement. However, third parties could also seek to hold us responsible for any of the liabilities that YUM has agreed to retain, and there can be no assurance that the indemnity from YUM will be sufficient to protect us against the full amount of such liabilities, or that YUM will be able to fully satisfy its indemnification obligations. In addition, YUM’s insurers may attempt to deny us coverage for liabilities associated with certain occurrences of indemnified liabilities prior to the separation. Moreover, even if we ultimately succeed in recovering from YUM or such insurance providers any amounts for which we are held liable, we may be temporarily required to bear these losses. Each of these risks could negatively affect our business, results of operations, financial condition and cash flows.

A court could require that we assume responsibility for obligations allocated to YUM under the separation and distribution agreement.

Under the separation and distribution agreement and related ancillary agreements, from and after the separation, each of YUM and the Company will be generally responsible for the debts, liabilities and other obligations related to the business or businesses which they own and operate following the consummation of the separation. Although we do not expect to be liable for any obligations that are not allocated to us under the separation and distribution agreement, a court could disregard the allocation agreed to between the parties, and require that we assume responsibility for obligations allocated to YUM (for example, tax and/or environmental liabilities), particularly if YUM were to refuse or were unable to pay or perform the allocated obligations.

Potential liabilities may arise due to fraudulent transfer considerations, which would adversely affect our results of operations and financial condition.

In connection with the separation and distribution, YUM completed several corporate reorganization transactions involving its subsidiaries which, along with the separation and distribution, may be subject to federal and state fraudulent conveyance and transfer laws. If, under these laws, a court were to determine that, at the time of the separation and distribution, any entity involved in these reorganization transactions or the separation and distribution:

- was insolvent;
- was rendered insolvent by reason of the separation and distribution or a related transaction;
- had remaining assets constituting unreasonably small capital; or
- intended to incur, or believed it would incur, debts beyond its ability to pay these debts as they matured,

then the court could void the separation and distribution, in whole or in part, as a fraudulent conveyance or transfer. The court could then require our stockholders to return to YUM some or all of the shares of Company common stock issued in the distribution, or require YUM or the Company, as the case may be, to fund liabilities of the other company for the benefit of creditors. The measure of insolvency will vary depending upon the jurisdiction whose law is being applied. Generally, however, an entity would be considered insolvent if the fair value of its assets was less than the amount of its liabilities, or if it was unable to pay its liabilities as they mature.

Certain of our executive officers and directors may have actual or potential conflicts of interest because of their previous positions at YUM.

Even though our board of directors consists of a majority of directors who are independent, and our executive officers who were employees of YUM ceased to be employees of YUM, some of our executive officers and directors continue to have a financial interest in YUM common stock and equity awards as a result of their former positions with YUM. Such ownership of YUM common stock or holding of YUM equity awards could create, or appear to create, potential conflicts of interest if the Company and YUM pursue the same corporate opportunities, have disagreements about the contracts between them or face decisions that could have different implications for the Company and YUM.

Risks Related to Our Common Stock

Our common stock has had relatively limited trading history, and the Company's stock price may fluctuate significantly.

There was no public market for our common stock prior to the distribution. The market price of Company common stock may decline or fluctuate significantly due to a number of factors, some of which may be beyond our control, including:

- actual or anticipated fluctuations in the our results of operations;
- significant liability claims, health concerns, food contamination complaints from our customers, shortages or interruptions in the availability of food or other supplies, or reports of incidents of food tampering;
- foreign exchange issues;
- the operating and stock price performance of comparable companies;
- changes in the Company's stockholder base due to the separation;
- changes in the regulatory and legal environment in which we operate; or
- market conditions in the restaurant industry and the domestic and worldwide economies as a whole.

The Company cannot guarantee the timing or amount of dividends on, or repurchases of, its common stock.

We intend to retain a significant portion of our earnings to finance the operation, development and growth of our business. Any future determination to declare and pay cash dividends will be at the discretion of our board of directors and will depend on, among other things, our financial condition, results of operations, actual or anticipated cash requirements, tax considerations, contractual or regulatory restrictions and such other factors as our board of directors deems relevant. Our board of directors has authorized a \$300 million share repurchase program. However, repurchases under the program will be at the discretion of management and we cannot guarantee the timing or amount of any share repurchases. For more information, see Item 5. "Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities."

Your percentage of ownership in the Company may be diluted in the future.

In the future, your percentage ownership in the Company may be diluted because of equity awards that we intend to grant to our directors, officers and employees or otherwise as a result of equity issuances for acquisitions or capital market transactions. The Company's and certain of YUM's employees have equity awards with respect to Company common stock as a result of conversion of their YUM equity awards (in whole or in part) to Company equity awards in connection with the distribution. Such awards will have a dilutive effect on the Company's earnings per share, which could adversely affect the market price of Company common stock. From time to time, the Company will issue additional stock-based awards to its employees under the Company's employee benefit plans.

In addition, our amended and restated certificate of incorporation authorizes us to issue, without the approval of the Company's stockholders, one or more classes or series of preferred stock that have such designation, powers, preferences and relative, participating, optional and other special rights, including preferences over Company common stock respecting dividends and distributions, as our board of directors generally may determine. The terms of one or more classes or series of preferred stock could dilute the voting power or reduce the value of Company common stock. Similarly, the repurchase or redemption rights or liquidation preferences we could assign to holders of preferred stock could affect the residual value of the common stock.

The interests of the Investors may differ from the interests of other holders of Company common stock, and the ownership percentage of other holders of Company common stock who received the shares of the Company's common stock in the distribution will be diluted as a result of the exercise of the warrants by the Investors.

In connection with the separation and distribution, the Investors received shares of common stock, representing approximately 4.8% of the outstanding shares of Company common stock as of February 28, 2017, or approximately 8.7% of the outstanding shares of Company common stock as of February 28, 2017 assuming the full exercise of warrants held by each of the Investors. The Company's full year 2016 earnings per share reflects only two months of impact from the shares issued to the Investors in connection with the separation and distribution, and such shares would have had an additional dilutive effect had they been outstanding for the full year 2016. Any shares issued as a result of the exercise of the warrants will have a dilutive effect on the Company's earnings per share, which could adversely affect the market price of Company common stock. In addition, the Investors have the ability to acquire additional shares of Company common stock in the open market (subject to an aggregate beneficial ownership interest limit of 19.9%).

The interests of the Investors may differ from those of other holders of Company common stock in material respects. For example, the Investors may have an interest in pursuing acquisitions, divestitures, financings or other transactions that could enhance their respective equity portfolios, even though such transactions might involve risks to holders of Company common stock. The Investors may, from time to time in the future, acquire interests in businesses that directly or indirectly compete with certain portions of the Company's business or are suppliers or customers of the Company. Additionally, the Investors may determine that the disposition of some or all of their interests in the Company would be beneficial to the Investors at a time when such disposition could be detrimental to the other holders of Company common stock.

Anti-takeover provisions in our organizational documents and Delaware law and our stockholder rights plan might discourage or delay acquisition attempts for us that you might consider favorable.

Our amended and restated certificate of incorporation and amended and restated bylaws and our stockholder rights plan contain provisions, summarized below, that could make it more difficult to acquire control of the Company by means of a tender offer, a proxy contest or otherwise, or to remove incumbent officers and directors. Further, as a Delaware corporation, we are subject to provisions of Delaware law, which may impair a takeover attempt that our stockholders may find beneficial. These provisions might discourage certain types of coercive takeover practices and takeover bids that our board of directors may consider inadequate or delay acquisition attempts for us that holders of Company common stock might consider favorable.

- The Company entered into a rights agreement with American Stock Transfer & Trust Company, LLC, as rights agent, which would impose a significant penalty upon any person or group that acquires 15% or more of the Company's outstanding common stock, without the approval of our board of directors. The rights agreement will automatically terminate without further action of our board of directors on the first anniversary of the distribution date.
- Our amended and restated certificate of incorporation provides that our board of directors is divided into three classes, with one-third of the directors being up for election at the 2017 annual meeting, one-third of the directors being up for election at the 2018 annual meeting and all of the directors being up for election at the 2019 annual meeting.
- Our amended and restated bylaws provide that, for so long as our board of directors is classified, stockholders may only remove our directors for cause. After the board of directors has been fully declassified, stockholders may remove our directors with or without cause.
- Our amended and restated bylaws provide that such bylaws may be amended by our board of directors or by the affirmative vote of a majority of our stockholders entitled to vote.
- Our amended and restated certificate of incorporation provides that only our board of directors (or the chairman of our board of directors, our chief executive officer or our secretary with the concurrence of a majority of our board of directors) may call special meetings of our stockholders.
- Our amended and restated certificate of incorporation expressly eliminates the right of our stockholders to act by written consent. Accordingly, stockholder action must take place at the annual or a special meeting of our stockholders.
- Our amended and restated bylaws establish advance notice procedures with respect to stockholder proposals and nomination of candidates for election as directors other than nominations made by or at the direction of our board of directors or a committee of our board of directors.
- Our amended and restated certificate of incorporation does not provide for cumulative voting, which means that stockholders are denied the right to cumulate votes in the election of directors.
- Our board of directors has the authority to issue preferred stock, which could potentially be used to discourage attempts by third parties to obtain control of our company through a merger, tender offer, proxy contest or otherwise by making such attempts more difficult or more costly.

Item 1B. Unresolved Staff Comments.

Not applicable.

Item 2. Properties.

As of year-end 2016, the Company leased land, building or both for 6,008 units in China, which unit count includes land use rights for approximately 38 properties. The Company-owned units are further detailed as follows:

- KFC leased land, building or both (including land use rights) for approximately 3,913 units.
- Pizza Hut Casual Dining leased land, building or both (including land use rights) for approximately 1,690 units.
- All Other Segments leased land, building or both (including land use rights) for approximately 405 units.

Company-owned restaurants in China are generally leased for initial terms of 10 to 20 years and generally do not have renewal options. The Company leases its corporate headquarters and test kitchen facilities in Shanghai, China and owns land use rights for six non-store properties of Little Sheep. The Company subleases approximately 180 properties to franchisees. Additional information about the Company's properties is included in Note 12 to the Consolidated and Combined Financial Statements in Part II, Item 8.

The Company believes that its properties are generally in good operating condition and are suitable for the purposes for which they are being used.

Item 3. Legal Proceedings.

The Company is subject to various lawsuits covering a variety of allegations from time to time. The Company believes that the ultimate liability, if any, in excess of amounts already provided for these matters in the Consolidated and Combined Financial Statements, is not likely to have a material adverse effect on the Company's annual results of operations, financial condition or cash flows. Matters faced by the Company from time to time include, but are not limited to, claims from landlords, employees, customers and others related to operational, contractual or employment issues. There were no material legal proceedings as of December 31, 2016.

Item 4. Mine Safety Disclosures.

Not applicable.

PART II

Item 5. Market for Registrant’s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.

Yum China common stock trades on the New York Stock Exchange (“NYSE”) under the symbol YUMC. Yum China common stock commenced trading on the NYSE on a “when-issued” basis on October 17, 2016 and began “regular-way” trading on November 1, 2016. Prior to October 17, 2016, there was no public market for Yum China common stock.

The following sets forth, for the period indicated, the high and low NYSE composite closing sale prices for Yum China common stock.

	2016	
Fiscal Quarter	High	Low
Fourth Quarter (from October 17, 2016 to December 31, 2016)	\$ 29.98	\$ 24.24

As of February 28, 2017, there were 50,903 holders of record of Yum China’s common stock. The number of registered holders does not include holders who are beneficial owners, but whose shares are held in street name by brokers and other nominees.

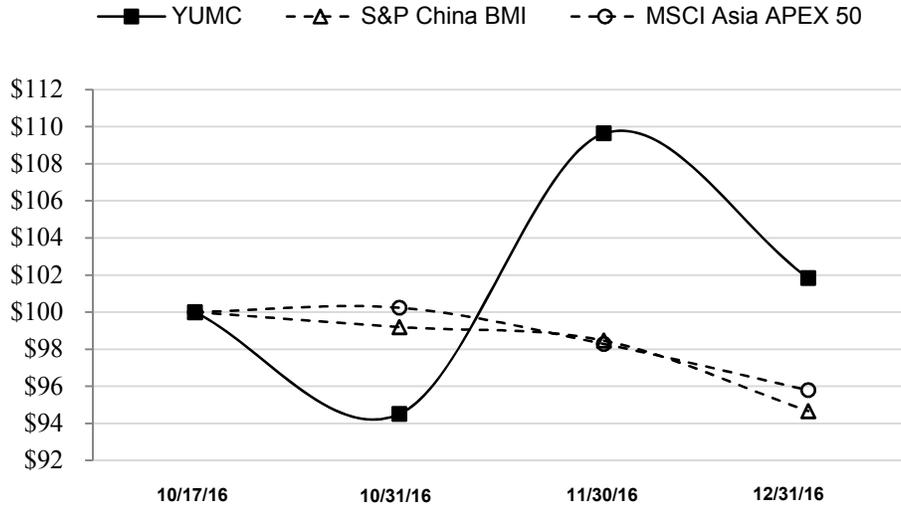
Dividends and Share Repurchases

Yum China has not paid any dividends or engaged in any share repurchases since the separation and distribution through the date on which this Form 10-K was filed with the SEC. We intend to retain a significant portion of our earnings to finance the operation, development and growth of our business. Any future determination to declare and pay cash dividends will be at the discretion of our board of directors and will depend on, among other things, our financial condition, results of operations, actual or anticipated cash requirements, contractual or regulatory restrictions, tax considerations and such other factors as our board of directors deems relevant. On February 7, 2017, we announced that our board of directors authorized a \$300 million share repurchase program. Yum China may repurchase shares under this program from time to time in open market or privately negotiated transactions, including block trades, accelerated share repurchase transactions and Rule 10b5-1 trading plans.

Our ability to declare and pay any dividends on our stock may be restricted by applicable Chinese laws. The laws, rules and regulations applicable to our Chinese subsidiaries permit payments of dividends only out of their accumulated profits, if any, determined in accordance with applicable Chinese accounting standards and regulations. Under Chinese law, an enterprise incorporated in China is required to set aside at least 10% of its after-tax profits each year, after making up previous years’ accumulated losses, if any, to fund certain statutory reserve funds, until the aggregate amount of such a fund reaches 50% of its registered capital. As a result, our Chinese subsidiaries are restricted in their ability to transfer a portion of their net assets to us in the form of dividends. At the discretion of the board of directors, as an enterprise incorporated in China, each of our Chinese subsidiaries may allocate a portion of its after-tax profits based on Chinese accounting standards to staff welfare and bonus funds. These reserve funds and staff welfare and bonus funds are not distributable as cash dividends.

Stock Performance Graph

This graph compares the cumulative total return of our common stock from October 17, 2016, which is the date “when-issued” trading in our common stock commenced, through December 31, 2016, with the comparable cumulative total return of the S&P China BMI and MSCI Asia APEX 50, a peer group that includes the Company. The graph assumes that the value of the investment in our common stock and each index was \$100 on October 17, 2016 and that all dividends were reinvested. We selected S&P China BMI and MSCI Asia APEX 50 for comparison, as YUMC is an index member of both of these indices.



\$100 Invested on 10/17/2016

	10/17/2016	10/31/2016	11/30/2016	12/31/2016
YUMC	\$ 100	\$ 95	\$ 110	\$ 102
S&P China BMI	\$ 100	\$ 99	\$ 98	\$ 95
MSCI Asia APEX 50	\$ 100	\$ 100	\$ 98	\$ 96

Item 6. Selected Financial Data.

The following table presents our selected historical consolidated and combined financial data. We derived the Consolidated and Combined Statements of Income (Loss) data and the Consolidated and Combined Cash Flows data for the years ended December 31, 2016, 2015 and 2014, and the Consolidated and Combined Balance Sheets data as of December 31, 2016 and 2015, as set forth below, from our audited Consolidated and Combined Financial Statements, which are included elsewhere in this Form 10-K. We derived the Combined Statements of Income (Loss) data and the Combined Cash Flows data for the year ended December 31, 2013, and the Combined Balance Sheets data as of December 31, 2014, as set forth below, from our audited Combined Financial Statements that are not included in this Form 10-K. We derived the Combined Statements of Income (Loss) data and the Combined Cash Flows data for the year ended December 31, 2012, and the Combined Balance Sheets data as of December 31, 2013 and 2012, as set forth below, from our unaudited Combined Financial Statements that are not included in this Form 10-K.

Our combined financial information for periods prior to the separation may not necessarily reflect our financial position, results of operations or cash flows as if we had operated as an independent public company during the periods prior to October 31, 2016, including changes that occurred in our operations and capitalization as a result of the separation from YUM and the distribution. Accordingly, our historical combined results should not be relied upon as an indicator of our future performance.

The following tables should be read together with, and are qualified in their entirety by reference to, the historical Consolidated and Combined Financial Statements and the related notes included elsewhere in this Form 10-K. Among other things, the historical Consolidated and Combined Financial Statements include more detailed information regarding the basis of presentation for the information in the following table. The tables should also be read together with the sections entitled “Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations” and “Item 8. Financial Statements and Supplementary Data.”

Selected Financial Data

Yum China Holdings, Inc.

(in US\$ millions, except per share and unit amounts)

	For the Years Ended December 31,				
	2016	2015	2014	2013	2012
Consolidated and Combined Statements of Income (Loss) Data:					
Revenues					
Company sales	\$ 6,622	\$ 6,789	\$ 6,821	\$ 6,800	\$ 6,797
Franchise fees and income	130	120	113	105	101
Total revenues	6,752	6,909	6,934	6,905	6,898
Costs and Expenses, Net					
Company restaurants					
Food and paper	1,919	2,159	2,207	2,258	2,312
Payroll and employee benefits	1,432	1,386	1,407	1,360	1,259
Occupancy and other operating expenses ^(a)	2,259	2,386	2,415	2,347	2,210
Company restaurant expenses	5,610	5,931	6,029	5,965	5,781
General and administrative expenses ^(b)	424	395	389	356	336
Franchise expenses ^(c)	71	70	64	60	55
Closures and impairment expenses, net	78	64	517	325	9
Refranchising gain, net ^(d)	(15)	(13)	(17)	(5)	(17)
Other income, net	(56)	(26)	(51)	(25)	(112)
Total costs and expenses, net	6,112	6,421	6,931	6,676	6,052
Operating Profit^(e)	640	488	3	229	846
Interest income, net	11	8	14	5	8
Changes in fair value of financial instruments	21	—	—	—	—
Income Before Income Taxes	672	496	17	234	854
Income tax provision	(158)	(168)	(54)	(135)	(181)
Net income (loss) – including noncontrolling interests	514	328	(37)	99	673
Net income (loss) – noncontrolling interests	12	5	(30)	(27)	11
Net Income (Loss) – Yum China Holdings, Inc.^(e)	502	323	(7)	126	662
Basic Earnings (Loss) Per Common Share	1.36	0.89	(0.02)	0.35	1.82
Diluted Earnings (Loss) Per Common Share	1.36	0.89	(0.02)	0.35	1.82
Diluted Earnings (Loss) Per Common Share before Special Items ^(f)	1.28	0.92	0.98	1.06	1.62
Consolidated and Combined Cash Flow Data:					
Net cash provided by operating activities	\$ 864	\$ 910	\$ 775	\$ 782	\$ 871
Capital spending	436	512	525	568	655
Consolidated and Combined Balance Sheet Data:					
Total assets	\$ 3,727	\$ 3,201	\$ 3,257	\$ 3,750	\$ 3,782
Property, plant and equipment, net	1,647	1,841	2,001	1,979	1,810
Total Equity – Yum China Holdings, Inc.	2,377	1,921	1,888	2,281	2,217
Other Data:					
Number of stores at year end					
Company	6,008	5,768	5,417	5,026	4,547
Unconsolidated Affiliates	836	796	757	716	660
Franchisees	718	612	541	501	519
Total	7,562	7,176	6,715	6,243	5,726
Total Company system sales growth ^(g)					
Reported	(1)%	—%	1%	(1)%	23%
Local currency ^(h)	5%	2%	1%	(4)%	20%
KFC system sales growth ^(g)					
Reported	—%	(2)%	(1)%	(7)%	17%
Local currency ^(h)	6%	—%	(1)%	(9)%	14%
Pizza Hut Casual Dining system sales growth ^(g)					
Reported	(2)%	8%	11%	28%	36%
Local currency ^(h)	3%	10%	12%	25%	32%

- (a) Occupancy and other operating expenses include license fees paid to YUM of \$199 million, \$219 million, \$217 million, \$215 million and \$217 million for the years ended December 31, 2016, 2015, 2014, 2013 and 2012, respectively.
- (b) General and administrative expenses include corporate expenses allocated from YUM of \$11 million, \$12 million, \$11 million, \$12 million and \$15 million for the years ended December 31, 2016, 2015, 2014, 2013 and 2012, respectively.
- (c) Franchise expenses include licenses fee paid to YUM of \$50 million, \$50 million, \$48 million, \$47 million and \$46 million for the years ended December 31, 2016, 2015, 2014, 2013 and 2012, respectively.
- (d) See Note 5 to the Consolidated and Combined Financial Statements for discussion of Refranchising gain, net.
- (e) Operating Profit for 2014 and 2013, respectively, includes \$463 million and \$295 million of expense associated with non-cash impairment of our investment in Little Sheep. After considering the tax benefit associated with these losses and the portion of the net losses allocated to noncontrolling interests, Net Income (Loss)—Yum China Holdings, Inc. was negatively impacted by these impairments by \$361 million and \$258 million in 2014 and 2013, respectively. Excluding these impairments, Net income (Loss)—Yum China Holdings, Inc. was income of \$354 million and \$384 million in 2014 and 2013, respectively. Operating profit in 2012 includes a \$74 million gain in 2012 related to the acquisition of additional interest in and resulting consolidation of Little Sheep with no associated tax expense. Excluding this gain, Net Income (Loss) —Yum China Holdings, Inc. was income of \$588 million in 2012.
- (f) In addition to the results provided in accordance with U.S. Generally Accepted Accounting Principles (“GAAP”) throughout this Form 10-K, the Company provides non-GAAP measurements which present certain operating results on a basis before Special Items. The Company uses Operating Profit before Special Items as a key performance measure of results of operations for the purpose of evaluating performance internally and Special Items are not included in any of our segment results. This non-GAAP measurement is not intended to replace the presentation of our financial results in accordance with GAAP. Rather, the Company believes that the presentation of Operating Profit before Special Items provides additional information to investors to facilitate the comparison of past and present results, excluding items that the Company does not believe are indicative of our ongoing operations due to their nature. 2016, 2015 and 2014 Special Items are described in further detail within our Management’s Discussion and Analysis of Financial Condition and Results of Operations. Special Items in 2013 negatively impacted Operating Profit by \$295 million due to the Little Sheep impairment. Special Items in 2012 positively impacted Operating Profit by \$74 million due to gain on the acquisition of an additional interest in and resulting consolidation of Little Sheep.
- (g) System sales growth includes the results of all restaurants regardless of ownership, including company-owned, unconsolidated affiliate and franchise restaurants that operate our Concepts, except for non-company-owned restaurants for which we do not receive a sales-based royalty. Sales of unconsolidated affiliate and franchise restaurants typically generate ongoing franchise fees for the Company at a rate of approximately 6% of system sales. Sales of unconsolidated affiliate and franchise restaurants are not included in the Company sales in the Consolidated and Combined Statements of Income (Loss); however, the franchise fees are included in the Company’s revenues. We believe system sales growth is useful to investors as a significant indicator of the overall strength of our business as it incorporates all of our revenue drivers, Company and franchise same-store sales as well as net unit growth.
- (h) Local currency represents the percentage change excluding the impact of foreign currency translation. These amounts are derived by translating current year results at prior year average exchange rates. We believe the elimination of the foreign currency translation impact provides better year-to-year comparability without distorting of foreign currency fluctuations.

Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations.

The following Management’s Discussion and Analysis (“MD&A”) should be read in conjunction with the Consolidated and Combined Financial Statements in Item 8, the “Forward-Looking Statements” section at the beginning of this Form 10-K and the “Risk Factors” section set forth in Item 1A.

All Note references in this MD&A refer to the Notes to the Consolidated and Combined Financial Statements included in Item 8. of this Form 10-K. Tabular amounts are displayed in millions of U.S. dollars except per share and unit count amounts, or as otherwise specifically identified. Percentages may not recompute due to rounding.

Basis of Presentation

The Company separated from YUM on October 31, 2016, becoming an independent, publicly traded company as a result of a pro rata distribution of all outstanding shares of Yum China common stock to shareholders of YUM. Accordingly, the financial statements presented in this Form 10-K represent (i) for periods prior to October 31, 2016, the combined financial statements of YUM’s China businesses and operations when Yum China was a wholly owned subsidiary of YUM (referred to as “Combined Financial Statements”) and (ii) for periods subsequent to October 31, 2016, the consolidated financial statements of the Company as a separate publicly traded company following its separation from YUM (referred to as “Consolidated Financial Statements”). Throughout this Form 10-K when we refer to the “financial statements,” we are referring to the “Consolidated and Combined Financial Statements,” unless the context indicates otherwise.

The Combined Financial Statements have been prepared on a standalone basis and are derived from YUM’s consolidated financial statements and underlying accounting records. Transactions between the Company and YUM that were not cash settled were considered to be effectively settled at the time the transactions are recorded. The Combined Financial Statements include all revenues, costs, assets and liabilities directly attributable to the Company either through specific identification or allocation. The Combined Statements of Income include allocations for certain of YUM’s Corporate functions which provide a direct benefit to the Company. These costs have been allocated based on Company system sales relative to YUM’s global system sales. All allocated costs have been deemed to have been paid to YUM in the period in which the costs were recorded. The Company considers the cost allocation methodology and results to be reasonable for the periods prior to October 31, 2016. However, the allocations may not be indicative of the actual expense that the Company would have experienced had the Company operated as an independent, publicly traded company for the periods prior to October 31, 2016. Upon the separation from YUM, Parent Company Investment was adjusted as a result of settlement of certain assets and liabilities with YUM and formed Yum China’s common stock and additional paid-in capital. See Note 2 to the Consolidated and Combined Financial Statements for further information.

Overview

We are the largest restaurant company in China, with over 7,500 restaurants as of year-end 2016, and \$6.8 billion of revenue, net income of \$502 million and \$1.13 billion of adjusted EBITDA in 2016. Our growing restaurant base consists of China’s leading restaurant concepts, including KFC, Pizza Hut Casual Dining, Pizza Hut Home Service, East Dawning, Little Sheep and Taco Bell. Following our separation from YUM, we have the exclusive right to operate and sub-license the KFC, Pizza Hut and, subject to achieving certain agreed upon milestones, Taco Bell brands in China, excluding Hong Kong, Taiwan and Macau, and we own the East Dawning and Little Sheep marks outright. We were the first major global restaurant brand to enter China in 1987 and we have developed deep operating experience in the market. We have since grown to become one of China’s largest retail developers covering over 1,100 cities and opening an average of approximately two new restaurants per day over the past five years.

Our KFC restaurants are the leading QSR brand in the PRC in terms of system sales and number of restaurants. As of December 31, 2016, KFC operated over 5,200 restaurants in over 1,100 cities across China. Measured by number of restaurants, we believe KFC has a two-to-one lead over the nearest Western QSR competitor in China and KFC continues to grow in both large and small cities. Similarly, Pizza Hut Casual Dining is the leading CDR concept in China as measured by system sales and number of restaurants. We believe Pizza Hut Casual Dining, with over 1,700 restaurants in over 400 cities as of December 31, 2016, has an approximately six-to-one lead in terms of restaurants over its nearest Western CDR competitor in China.

The operations of each of the Concept represent an operating segment of the Company within these Consolidated and Combined Financial Statements. We have two reportable segments: KFC and Pizza Hut Casual Dining. Our remaining operating segments, including the operations of Pizza Hut Home Service, East Dawning, Little Sheep and Taco Bell, are combined and referred to as All Other Segments, as those operating segments are insignificant both individually and in the aggregate.

We intend for this MD&A to provide the reader with information that will assist in understanding our results of operations, including metrics that management uses to assess the Company's performance. Throughout this MD&A, we discuss the following performance metrics:

- The Company provides certain percentage changes excluding the impact of foreign currency translation ("F/X"). These amounts are derived by translating current year results at prior year average exchange rates. We believe the elimination of the F/X impact provides better year-to-year comparability without the distortion of foreign currency fluctuations.
- System sales growth includes the results of all restaurants regardless of ownership, including Company-owned, franchise and unconsolidated affiliate restaurants that operate our Concepts, except for non-company-owned restaurants for which we do not receive a sales-based royalty. Sales of franchise and unconsolidated affiliate restaurants typically generate ongoing franchise fees for the Company at a rate of approximately 6% of system sales. Franchise and unconsolidated affiliate restaurant sales are not included in Company sales on the Consolidated and Combined Statements of Income; however, the franchise fees are included in the Company's revenues. We believe system sales growth is useful to investors as a significant indicator of the overall strength of our business as it incorporates all of our revenue drivers, Company and franchise same-store sales as well as net unit growth.
- Same-store sales growth is the estimated percentage change in sales of all restaurants that have been open and in the Company system one year or more.
- Company Restaurant profit ("Restaurant profit") is defined as Company sales less expenses incurred directly by our Company-owned restaurants in generating Company sales. Company restaurant margin as a percentage of sales is defined as Restaurant profit divided by Company sales. Within the Company Sales and Restaurant Profit analysis, Store Portfolio Actions represent the net impact of new unit openings, acquisitions, refranchising and store closures, and Other primarily represents the impact of same-store sales as well as the impact of changes in costs such as inflation/deflation.

- In addition to the results provided in accordance with GAAP throughout this MD&A, the Company provides non-GAAP measurements which present Operating Profit before Special Items, Diluted Earnings (Loss) Per Common Share before Special Items, effective tax rate before Special Items and Adjusted EBITDA. Included in Special Items are reversal of (provision for) losses associated with sales of aircraft, incremental restaurant-level impairment upon separation, changes in fair value of financial instruments and impact of the redemption of the Little Sheep noncontrolling interest. The Company excludes impact from Special Items for the purpose of evaluating performance internally. Special Items are not included in any of our segment results. These non-GAAP measures are not intended to replace the presentation of our financial results in accordance with GAAP. Rather, the Company believes that the presentation of these non-GAAP measures provides additional information to investors to facilitate the comparison of past and present results, excluding those items that the Company does not believe are indicative of our ongoing operations due to their nature.

Results of Operations

Summary

All comparisons within this summary are versus the same period a year ago and exclude the impact of Special Items. All system sales growth, same-store sales growth and Operating Profit comparisons exclude the impact of foreign currency. Refer to Item 1. Business for a discussion on the seasonality of our operations.

In 2014, the Company's sales and profits were significantly impacted by adverse publicity surrounding improper food handling practices by a former supplier. Specifically, on July 20, 2014, an undercover report was televised in China depicting improper food handling practices by supplier Shanghai Husi, a division of OSI, which is a large, global supplier to many in the restaurant industry. This triggered extensive news coverage in China that shook consumer confidence and impacted brand usage. Immediately following the incident, we experienced a significant, negative impact to sales and profits at both KFC and Pizza Hut Casual Dining. For further information about the potential impact of food safety risks on our business, see "Item 1A. Risk Factors—Risks Related to Our Business and Industry—Food safety and food-borne illness concerns may have an adverse effect on our reputation and business."

In 2015, our sales and profits continued to be negatively impacted by the adverse publicity in July 2014. Sales initially turned significantly positive as we lapped the supplier incident, but overall sales in the second half of 2015 trailed our expectations, particularly at Pizza Hut Casual Dining. In the second half of 2015, KFC grew same-store sales 3% in the third quarter and 6% in the fourth quarter, which was below our forecasts. Over the same period, Pizza Hut Casual Dining experienced same-store sales declines of 1% in the third quarter and 8% in the fourth quarter. We believe that this performance was driven primarily by (1) extraordinary volatility in financial markets, currency devaluation and overall softer economic conditions which weigh more heavily on the casual dining sector; (2) the impact of online delivery aggregators entering the casual dining space; and (3) marketing promotions which underperformed our expectations.

In 2016, the Company's sales, excluding F/X, improved, as same-store sales turned around with positive trend, reversing a three-year period of declines. The Company overcame challenges arising from an international court ruling in July 2016 regarding claims to sovereignty over the South China Sea that triggered a series of regional protests and boycotts, intensified by social media, against a few international companies with well-known Western brands. The growth in Company's profit was primarily aided by the impact of the retail tax structure reform implemented on May 1, 2016. The benefit from the retail tax structure reform was most visible and impactful on food and paper costs while other items such as utility cost and rental expense also benefited from it. For further information about the potential impact political, regulatory, economic and social conditions in China may have on our business, see "Item 1A. Risks Related to Doing Business in China—Changes in Chinese political policies and economic and social policies or conditions may materially and adversely affect our business, results of operations and financial condition and may result in our inability to sustain our growth and expansion strategies."

2016 financial highlights are below:

	KFC	Pizza Hut Casual Dining	All other Segments	Total
System Sales Growth (Decline) ^(a)	6%	3%	(6)%	5%
Operating Profit Growth (Decline) ^(a)	36%	11%	54%	38%
Same Store Sales Growth (Decline) ^(a)	3%	(7)%	(5)%	—%
New Unit Openings	323	178	74	575

(a) System Sales, Operating Profit and Same-Store Sales percentages as shown in 2016 financial highlights exclude the impact of F/X.

The Consolidated and Combined Results of Operations for the years ended December 31, 2016, 2015 and 2014 are presented below:

	Year			% B/(W) ^(a)	
	2016	2015	2014	2016	2015
Company sales	\$ 6,622	\$ 6,789	\$ 6,821	(2)	—
Franchise fees and income	130	120	113	8	7
Total revenues	<u>\$ 6,752</u>	<u>\$ 6,909</u>	<u>\$ 6,934</u>	(2)	—
Restaurant profit	<u>\$ 1,012</u>	<u>\$ 858</u>	<u>\$ 792</u>	18	8
Restaurant margin %	<u>15.3%</u>	<u>12.6%</u>	<u>11.6%</u>	2.7 ppts.	1.0 ppts.
Operating Profit	\$ 640	\$ 488	\$ 3	31	NM
Interest income, net	11	8	14	50	(46)
Changes in fair value of financial instruments	21	—	—	NM	—
Income tax provision	(158)	(168)	(54)	6	NM
Net income (loss) – including noncontrolling interests	514	328	(37)	57	NM
Net income (loss) – noncontrolling interests	12	5	(30)	NM	NM
Net Income (Loss) – Yum China Holdings, Inc.	<u>\$ 502</u>	<u>\$ 323</u>	<u>\$ (7)</u>	55	NM
Diluted Earnings (Loss) Per Common Share ^(a)	<u>\$ 1.36</u>	<u>\$ 0.89</u>	<u>\$ (0.02)</u>	53	NM
Reported Effective tax rate	<u>23.5%</u>	<u>33.9%</u>	<u>322.3%</u>		
Operating Profit before Special Items	<u>\$ 655</u>	<u>\$ 503</u>	<u>\$ 466</u>		
Diluted Earnings (Loss) Per Common Share before Special Items	<u>\$ 1.28</u>	<u>\$ 0.92</u>	<u>\$ 0.98</u>		
Effective tax rate before Special Items	<u>26.2%</u>	<u>33.7%</u>	<u>26.8%</u>		
Adjusted EBITDA	<u>\$ 1,127</u>	<u>\$ 998</u>	<u>\$ 931</u>		

(a) Represents year-over-year change in percentage. NM refers to changes over 100%, from negative to positive amounts or from zero to an amount.

Performance Metrics

	2016	2015
System Sales Growth (Decline)	(1)%	—%
System Sales Growth, excluding F/X	5%	2%
Same-store Sales Growth (Decline)	—%	(4)%

<u>Unit Count</u>				% Increase	
	2016	2015	2014	2016	2015
Company-owned	6,008	5,768	5,417	4	6
Unconsolidated affiliates	836	796	757	5	5
Franchise	718	612	541	17	13
	<u>7,562</u>	<u>7,176</u>	<u>6,715</u>	5	7

Special Items

Special Items, along with the reconciliation to the most comparable GAAP financial measure, are presented below.

Detail of Special Items	Year		
	2016	2015	2014
Little Sheep impairment (See Note 5)	\$ —	\$ —	\$ (463)
Reversal of (provision for) losses associated with sale of aircraft ^(a) (See Note 5)	2	(15)	—
Incremental restaurant-level impairment upon separation ^(b) (See Note 5)	(17)	—	—
Special Items Expense - Operating Profit	(15)	(15)	(463)
Changes in fair value of financial instruments ^(c) (See Note 11)	21	—	—
Tax benefit on Special Items ^(d)	16	4	76
Special Items income (expense), net of tax - including noncontrolling interests	22	(11)	(387)
Special Items income (expense), net of tax - noncontrolling interests ^(e)	(8)	—	(26)
Special Items Income (Expense), net of tax - Yum China Holdings, Inc.	\$ 30	\$ (11)	\$ (361)
Weighted average diluted shares outstanding	369,143,838	363,758,219	363,758,219
Special Items Diluted Earnings (Loss) Per Common Share	\$ 0.08	\$ (0.03)	\$ (1.00)
Reconciliation of Reported Operating Profit to Operating Profit Before Special Items			
Reported Operating Profit	\$ 640	\$ 488	\$ 3
Special Items Expense - Operating Profit	(15)	(15)	(463)
Operating Profit before Special Items	\$ 655	\$ 503	\$ 466
Reconciliation of Reported EPS to EPS Before Special Items			
Reported Diluted Earnings (Loss) Per Common Share	\$ 1.36	\$ 0.89	\$ (0.02)
Special Items Diluted Earnings (Loss) Per Common Share	0.08	(0.03)	(1.00)
Diluted Earnings (Loss) Per Common Share before Special Items	\$ 1.28	\$ 0.92	\$ 0.98
Reconciliation of Reported Effective Tax Rate to Effective Tax Rate Before Special Items			
Reported effective tax rate (See Note 17)	23.5%	33.9%	322.3%
Impact on tax rate as a result of Special Items ^(d)	(2.7)%	0.2%	295.5%
Effective tax rate before Special Items	26.2%	33.7%	26.8%

(a) During 2015, we made the decision to dispose of a corporate aircraft in China and recognized a loss of \$15 million associated with the planned sale of the aircraft for the year ended December 31, 2015. We completed the sale during 2016. The sale proceeds of \$19 million was greater than the net book value of \$17 million of the aircraft at the time of disposal, which resulted in the reversal of \$2 million of the previously recognized loss.

(b) Incremental restaurant-level impairment represents additional impairment as a result of including the impact from the license fee paid to YUM on the individual restaurants future cash flow, which is equal to 3% of net system sales. Such license fee did not impact the impairment assessment prior to the separation as it was considered an intercompany charge at the time, whereas it became a charge from a third party after the separation and, therefore, should be considered in the impairment assessment.

- (c) In connection with the investment agreement with strategic investors entered into on September 1, 2016, Yum China issued 19,145,169.42 shares of common stock on November 1, 2016, subject to potential adjustment (“Post-Closing Adjustment”) by December 30, 2016, and warrants to purchase additional shares of common stock. The Post-Closing Adjustment and the warrants were accounted for as derivative instruments and liability-classified equity contracts, respectively. These financial instruments were initially measured at fair value on the date of issuance, with subsequent changes in fair value of \$21 million recognized in earnings during the year ended December 31, 2016. No subsequent fair value measurements were recognized after December 30, 2016. (See Note 11)
- (d) The tax benefit was determined based upon the impact of the nature of each Special Item tax effected at the 25% China tax rate or the 35% US tax rate, except for the \$21 million changes in fair value of financial instruments associated with the strategic investment which resulted in no income tax expense. Additionally, during the year ended December 31, 2016, we recognized a tax benefit of \$26 million related to the legal entity restructuring of our Little Sheep business by YUM. \$12 million of this benefit was attributed to previous Little Sheep impairment losses recognized within Special Items in 2014 and 2013 and as such was classified as a Special Item consistent with the classification of those historical impairments.
- (e) During the year ended December 31, 2016, the Little Sheep founding shareholders sold their remaining 7% Little Sheep ownership interest to the Company pursuant to their redemption rights. The difference between the purchase price of less than \$1 million, which was determined using a non-fair value based formula pursuant to the agreement governing the redemption rights, and the carrying value of their redeemable noncontrolling interests was recorded as an \$8 million loss attributable to noncontrolling interests. (See Note 8)

Adjusted EBITDA

Reported net income (loss), along with the reconciliation to Adjusted EBITDA, is presented below.

	2016	2015	2014
Reconciliation of Reported Net Income (Loss) to Adjusted EBITDA			
Net Income (Loss)—Yum China Holdings, Inc.	\$ 502	\$ 323	\$ (7)
Net income (loss)—noncontrolling interests	12	5	(30)
Income tax provision	158	168	54
Interest income, net	(11)	(8)	(14)
Changes in fair value of financial instruments	(21)	—	—
Reported Operating Profit	640	488	3
Depreciation and amortization	402	425	411
Store impairment charges (See Note 5)	70	70	54
Special Items Expense—Operating Profit	15	15	463
Adjusted EBITDA	<u>\$ 1,127</u>	<u>\$ 998</u>	<u>\$ 931</u>

Segment Results

KFC

				% B/(W)		% B/(W)	
	2016	2015	2014	2016		2015	
				Reported	Ex F/X	Reported	Ex F/X
Company sales	\$ 4,572	\$ 4,652	\$ 4,782	(2)	4	(3)	(1)
Franchise fees and income	124	116	111	7	13	4	7
Total revenues	<u>4,696</u>	<u>4,768</u>	<u>4,893</u>	(2)	4	(3)	(1)
Restaurant profit	\$ 746	\$ 620	\$ 559	20	27	11	14
Restaurant margin %	16.3%	13.3%	11.7%	3.0 ppts.	3.0 ppts.	1.6 ppts.	1.7 ppts.
G&A expenses	\$ 161	\$ 150	\$ 150	(7)	(13)	—	(2)
Closure and impairment expenses, net	\$ 41	\$ 50	\$ 41	18	13	(22)	(26)
Other income, net	\$ (45)	\$ (33)	\$ (21)	37	45	61	61
Operating Profit	\$ 645	\$ 499	\$ 435	29	36	14	18

	2016	2015
System Sales Growth (Decline)	—%	(2)%
System Sales Growth, excluding F/X	6%	—%
Same-Store Sales Growth (Decline)	3%	(4)%

Unit Count	% Increase				
	2016	2015	2014	2016	2015
Company-owned	3,913	3,821	3,732	2	2
Unconsolidated affiliates	836	796	757	5	5
Franchise	475	386	339	23	14
	<u>5,224</u>	<u>5,003</u>	<u>4,828</u>	4	4

	2015	New Builds	Closures	Refranchised	Acquired	2016
Company-owned	3,821	251	(87)	(73)	1	3,913
Unconsolidated affiliates	796	56	(9)	(7)	—	836
Franchise	386	16	(6)	80	(1)	475
Total	<u>5,003</u>	<u>323</u>	<u>(102)</u>	<u>—</u>	<u>—</u>	<u>5,224</u>

	2014	New Builds	Closures	Refranchised	Acquired	Other	2015
Company-owned	3,732	282	(144)	(52)	3	—	3,821
Unconsolidated affiliates	757	58	(15)	—	—	(4)	796
Franchise	339	11	(17)	52	(3)	4	386
Total	<u>4,828</u>	<u>351</u>	<u>(176)</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>5,003</u>

Company Sales and Restaurant Profit

The changes in Company sales and Restaurant profit were as follows:

<u>Income (Expense)</u>	2016 vs. 2015				2016
	2015	Store Portfolio		F/X	
		Actions	Other		
Company sales	\$ 4,652	\$ 59	\$ 122	\$ (261)	\$ 4,572
Cost of sales	(1,512)	(11)	77	78	(1,368)
Cost of labor	(903)	(11)	(73)	54	(933)
Occupancy and other operating expenses	(1,617)	(9)	14	87	(1,525)
Restaurant profit	<u>\$ 620</u>	<u>\$ 28</u>	<u>\$ 140</u>	<u>\$ (42)</u>	<u>\$ 746</u>

<u>Income (Expense)</u>	2015 vs. 2014				2015
	2014	Store Portfolio		F/X	
		Actions	Other		
Company sales	\$ 4,782	\$ 137	\$ (176)	\$ (91)	\$ 4,652
Cost of sales	(1,584)	(40)	83	29	(1,512)
Cost of labor	(963)	(18)	60	18	(903)
Occupancy and other operating expenses	(1,676)	(42)	69	32	(1,617)
Restaurant profit	<u>\$ 559</u>	<u>\$ 37</u>	<u>\$ 36</u>	<u>\$ (12)</u>	<u>\$ 620</u>

In 2016, the increase in Company sales and Restaurant profit associated with store portfolio actions was driven by net new unit growth, partially offset by the impact of more franchising. Significant other factors impacting Company sales and/or Restaurant profit were the favorable impact of cost favorability from retail tax structure reform (primarily in cost of sales), Company same-store sales growth of 3% and lower utility cost, partially offset by higher labor costs including wage inflation of 8%, and commodity inflation of 1%.

In 2015, the increase in Company sales and Restaurant profit associated with store portfolio actions was driven by net new unit growth, partially offset by the impact of franchising. Significant other factors impacting Company sales and/or Restaurant profit were labor efficiencies and lower utilities, partially offset by wage inflation of 8% and Company same-store sales declines of 4%.

Franchise Fees and Income

In 2016, the increase in Franchise fees and income, excluding the impact of F/X, was driven by the impact of franchising.

In 2015, the increase in Franchise fees and income, excluding the impact of F/X, was driven by the impact of franchising and net new unit growth, partially offset by franchise same-store sales declines of 9%.

G&A Expenses

In 2016, the increase in G&A expenses, excluding the impact of F/X, was driven by higher compensation costs due to wage inflation and higher incentive compensation associated with better operating results of KFC.

In 2015, the increase in G&A expenses, excluding the impact of F/X, was driven by higher compensation costs due to wage inflation.

Operating Profit

In 2016, the increase in Operating Profit, excluding the impact of F/X, was driven by the impact of same-store sales growth, lower restaurant operating costs, including the favorable impact of the retail tax structure reform and net new unit growth, partially offset by higher G&A expenses. In addition, the leap year in 2016 added an extra day in February resulting in incremental Operating Profit of \$5 million.

In 2015, the increase in Operating Profit, excluding the impact of F/X, was driven by net new unit growth and lower restaurant operating costs, partially offset by same-store sales declines and higher closure and impairment expenses.

Pizza Hut Casual Dining

	2016	2015	2014	% B/(W) 2016		% B/(W) 2015	
				Reported	Ex F/X	Reported	Ex F/X
Company sales	\$1,772	\$1,824	\$1,696	(3)	3	8	10
Franchise fees and income	2	1	—	NM	NM	NM	NM
Total revenues	<u>\$1,774</u>	<u>\$1,825</u>	<u>\$1,696</u>	(3)	3	8	10
Restaurant profit	\$ 248	\$ 225	\$ 243	10	17	(7)	(5)
Restaurant margin %	14.0%	12.3%	14.3%	1.7 ppts.	1.7 ppts.	(2.0)ppts.	(1.9)ppts.
G&A expenses	\$ 80	\$ 73	\$ 65	(10)	(16)	(12)	(14)
Closure and impairment expenses, net	\$ 17	\$ 8	\$ 2	NM	NM	NM	NM
Operating Profit	\$ 150	\$ 145	\$ 176	4	11	(18)	(16)

	2016	2015
System Sales Growth (Decline)	(2)%	8%
System Sales Growth, excluding F/X	3%	10%
Same-Store Sales Growth (Decline)	(7)%	(5)%

Unit Count	2016	2015	2014	% Increase	
				2016	2015
Company-owned	1,690	1,556	1,310	9	19
Franchise	24	16	3	50	NM
	<u>1,714</u>	<u>1,572</u>	<u>1,313</u>	9	20

	2015	New Builds	Closures	Refranchised	2016
Company-owned	1,556	173	(36)	(3)	1,690
Franchise	16	5	—	3	24
Total	<u>1,572</u>	<u>178</u>	<u>(36)</u>	<u>—</u>	<u>1,714</u>

	2014	New Builds	Closures	Refranchised	2015
Company-owned	1,310	279	(21)	(12)	1,556
Franchise	3	1	—	12	16
Total	<u>1,313</u>	<u>280</u>	<u>(21)</u>	<u>—</u>	<u>1,572</u>

Company Sales and Restaurant Profit

The changes in Company sales and Restaurant profit were as follows:

<u>Income (Expense)</u>	2016 vs. 2015				2016
	2015	Store Portfolio Actions	Other	F/X	
Company sales	\$ 1,824	\$ 172	\$ (122)	\$ (102)	\$ 1,772
Cost of sales	(543)	(44)	97	26	(464)
Cost of labor	(391)	(46)	(2)	24	(415)
Occupancy and other operating expenses	(665)	(62)	45	37	(645)
Restaurant profit	<u>\$ 225</u>	<u>\$ 20</u>	<u>\$ 18</u>	<u>\$ (15)</u>	<u>\$ 248</u>

<u>Income (Expense)</u>	2015 vs. 2014				2015
	2014	Store Portfolio Actions	Other	F/X	
Company sales	\$ 1,696	\$ 249	\$ (85)	\$ (36)	\$ 1,824
Cost of sales	(494)	(75)	15	11	(543)
Cost of labor	(346)	(58)	5	8	(391)
Occupancy and other operating expenses	(613)	(95)	30	13	(665)
Restaurant profit	<u>\$ 243</u>	<u>\$ 21</u>	<u>\$ (35)</u>	<u>\$ (4)</u>	<u>\$ 225</u>

In 2016, the increase in Company sales and Restaurant profit associated with store portfolio actions was driven by net new unit growth. Significant other factors impacting Company sales and/or Restaurant profit were the favorable impact from retail tax structure reform (primarily in cost of sales) and commodity deflation of 3%, partially offset by Company same-store sales declines of 7% and higher labor costs including wage inflation of 9%.

In 2015, the increase in Company sales and Restaurant profit associated with store portfolio actions was driven by net new unit growth. Significant other factors impacting Company sales and/or Restaurant profit were wage rate inflation of 8% and Company same-store sales declines of 5%, partially offset by labor efficiencies and lower utilities.

G&A Expenses

In 2016, the increase in G&A expenses, excluding the impact of F/X, was driven by higher compensation costs due to wage rate inflation and higher headcount.

In 2015, the increase in G&A expenses, excluding the impact of F/X, was driven by higher compensation costs due to wage rate inflation and higher headcount.

Operating Profit

In 2016, the increase in Operating Profit, excluding the impact of F/X, was driven by lower restaurant operating costs, including the favorable impact of the retail tax structure reform, and net new unit growth, partially offset by same-store sales declines of 7% and higher G&A expenses.

In 2015, the decrease in Operating Profit, excluding the impact of F/X, was driven by higher restaurant operating costs, same-store sales declines and higher G&A expenses, partially offset by net new unit growth.

All Other Segments

All Other Segments includes Pizza Hut Home Service, East Dawning, Little Sheep and Taco Bell.

				% B/(W)		% B/(W)	
	2016	2015	2014	2016		2015	
				Reported	Ex F/X	Reported	Ex F/X
Company sales	\$ 278	\$ 313	\$ 343	(11)	(6)	(9)	(7)
Franchise fees and income	4	3	2	18	25	NM	NM
Total revenues	<u>\$ 282</u>	<u>\$ 316</u>	<u>\$ 345</u>	<u>(11)</u>	<u>(5)</u>	<u>(8)</u>	<u>(6)</u>
Restaurant profit	\$ 17	\$ 13	\$ (10)	32	41	NM	NM
Restaurant margin %	6.4%	4.3%	(2.8)%	2.1 ppts.	2.1 ppts.	7.1 ppts.	7.2 ppts.
G&A expenses	\$ 30	\$ 28	\$ 31	(6)	(12)	7	5
Closure and impairment expenses, net	\$ 3	\$ 6	\$ 11	44	40	44	43
Operating Loss	\$ (6)	\$ (14)	\$ (44)	55	54	70	70

In 2016, the decrease in total revenues, excluding the impact of F/X, was driven by same-store sales declines of 5% and unit closures and refranchising related to Little Sheep, partially offset by net new unit growth.

In 2015, the decrease in total revenues, excluding the impact of F/X, was driven by unit closures, refranchising and same-store sales declines related to Little Sheep units, partially offset by net new unit growth and same-store sales growth for Pizza Hut Home Service.

In 2016, the decrease in Operating Loss, excluding the impact of F/X, was driven by lower operating losses at Pizza Hut Home Service and Little Sheep.

In 2015, the decrease in Operating Loss, excluding the impact of F/X, was driven by lower operating losses at Little Sheep.

Corporate & Unallocated

<u>Income (Expense)</u>	2016	2015	2014	% B/(W)	
				2016	2015
Corporate G&A expenses	(153)	\$ (144)	\$ (143)	(6)	(1)
Unallocated closures and impairments (See Note 5)	(17)	—	(463)	NM	NM
Refranchising gain (See Note 5)	15	13	17	9	(21)
Other unallocated (See Note 7)	6	(11)	25	NM	(43)
Interest income, net	11	8	14	50	(46)
Income tax provision (See Note 17)	(158)	(168)	(54)	6	NM
Effective tax rate (See Note 17)	23.5%	33.9%	322.3%	10.4 ppts.	NM

Corporate G&A Expenses

In 2016, the increase in Corporate G&A expenses was driven by higher compensation costs due to higher incentive compensation associated with better operating results of the Company and wage inflation, and the expenses associated with becoming an independent, publicly listed company.

In 2015, the increase in Corporate G&A expenses was driven by higher compensation costs due to wage inflation and higher headcount.

Unallocated Closures and Impairments

In 2016, unallocated closures and impairments represent the restaurant-level incremental impairment expense of \$17 million associated with the 3% license fee paid to YUM which was not included in our restaurant impairment indicator and recoverability tests prior to the separation. See Note 5.

Other Unallocated

In 2016, Other unallocated primarily includes the reversal of loss associated with the disposal of a corporate aircraft and insurance recoveries related to the 2012 poultry supply incident. See Note 7.

In 2015, Other unallocated primarily includes the write-down related to our decision to dispose of a corporate aircraft, partially offset by insurance recoveries related to the 2012 poultry supply incident.

Interest Income, Net

The increase in interest income, net for 2016 was driven by higher returns on short-term investments and time deposits.

The decrease in interest income, net for 2015 was driven by lower returns on short-term investments.

Income Tax Provision

Our income tax provision includes tax on our earnings at the Chinese statutory tax rate of 25%. To the extent those earnings are not deemed permanently reinvested in China, we are required to record U.S. tax on those earnings, net of a credit for the foreign taxes paid in China. Our effective tax rate was 23.5%, 33.9% and 322.3% in 2016, 2015 and 2014, respectively. The lower effective tax rate in 2016 was due to the recognition of tax benefit of \$26 million as a result of the legal entity restructuring of our Little Sheep business. The higher effective tax rate in 2014 was primarily due to the recognition of \$160 million of non-cash Little Sheep goodwill impairment, which resulted in no related tax benefit.

Significant Known Events, Trends or Uncertainties Expected to Impact Future Results

PRC Value-Added Tax

Effective May 1, 2016, the Chinese government implemented reform to its retail tax structure, which is intended to be a progressive and positive shift to more closely align with a more modern service-based economy. Under this reform, a 6% output VAT replaced the 5% Business Tax previously applied to certain restaurant sales. Input VAT would be creditable to the aforementioned 6% output VAT.

Entities that are VAT general taxpayers are permitted to offset qualified input VAT paid to suppliers against their output VAT upon receipt of appropriate supplier VAT invoices on an entity by entity basis. When the output VAT exceeds the input VAT, the difference is remitted to tax authorities, usually on a monthly basis; whereas when the input VAT exceeds the output VAT, the difference is treated as an input VAT credit asset which can be carried forward indefinitely to offset future net VAT payables. VAT related to purchases and sales which have not been settled at the balance sheet date is disclosed separately as an asset and liability, respectively, in the Consolidated and Combined Balance Sheets. At each balance sheet date, the Company reviews the outstanding balance of any input VAT credit asset for recoverability based on its forecasted operating results. As of December 31, 2016, an input VAT credit asset of \$80 million and payable of \$3 million were recorded in Other assets and Accounts payable and other current liabilities, respectively, in the Consolidated and Combined Balance Sheets.

Our restaurant margins benefited from the VAT reform in the year ended December 31, 2016 and we expect a positive financial benefit under this VAT regime going forward. However, the amount of our expected benefit from this VAT regime depends on a number of factors, some of which are outside of our control. The VAT reform is still at an early stage of implementation and the interpretation and application of the new VAT regime may not be immediately clear or settled at some local governmental levels. In addition, the timetable for enacting the prevailing VAT regulations into national VAT law, including ultimate enacted VAT rates, is not clear. As a result, for the foreseeable future, the benefit of this significant and complex VAT reform has the potential to fluctuate from quarter to quarter.

Foreign Currency Exchange Rate

The reporting currency of the Company is the US\$. Most of the revenues, costs, assets and liabilities of the Company are denominated in RMB. Any significant change in the exchange rate between US\$ and RMB may materially and adversely affect the Company's business, results of operations, cash flows and financial condition. See "Item 7A. Quantitative and Qualitative Disclosures About Market Risk" for a further discussion.

Consolidated and Combined Cash Flows

Net cash provided by operating activities was \$864 million in 2016 as compared to \$910 million in 2015. The decrease was primarily driven by increased inventory procurement and timing of payments for inventory, and a related increase in accounts receivable driven by amounts due from franchisees and unconsolidated affiliates as the Company adopted a central procurement model in August 2016, and an increase in VAT credit asset associated with the benefit from the retail tax structure reform, partially offset by higher Operating Profit.

In 2015, net cash provided by operating activities was \$910 million as compared to \$775 million in 2014. The increase was primarily due to the timing of payments for inventory, lower tax payments and higher Operating Profit.

Net cash used in investing activities was \$471 million in 2016 as compared to \$493 million in 2015. The decrease was primarily driven by lower capital spending, partially offset by increased purchases of short-term investments.

In 2015, net cash used in investing activities was \$493 million as compared to \$512 million in 2014. The decrease was primarily driven by lower capital spending.

Net cash provided by financing activities was \$95 million in 2016 as compared to net cash used in financing activities of \$213 million in 2015. The increase was primarily driven by proceeds from issuance of common stock and warrants, partially offset by changes in net parent investment.

In 2015, net cash used in financing activities was \$213 million in 2015 as compared to \$319 million in 2014. The decrease was primarily driven by changes in net parent investment.

Liquidity and Capital Resources

Historically we have funded our operations through cash generated from the operation of our Company-owned stores and from our franchise operations and dividend payments from our unconsolidated affiliates. Excess cash has historically been repatriated to YUM through intercompany loans or dividends.

Our ability to fund our future operations and capital needs will depend on our ongoing ability to generate cash from operations. We believe our principal uses of cash in the future will be primarily to fund our operations, capital expenditures and any distributions to our stockholders or share repurchases we may make. We believe that our future cash from operations, together with our access to funds on hand and capital markets, will provide adequate resources to fund these uses of cash and that our existing cash and net cash from operations will be sufficient to fund our operations and anticipated capital expenditures for the next 12 months.

Our balance sheet may reflect a working capital deficit, which is not uncommon in our industry and is also historically common for YUM. Company sales are paid for in cash or by credit card or mobile payment (which is quickly converted into cash). Substantial amounts of cash received from our restaurant operations are invested in new restaurant assets which are non-current in nature. As part of our working capital strategy, we negotiate favorable credit terms with vendors although our on-hand inventory turns slightly slower than the related short-term liabilities. Accordingly, it is not unusual for current liabilities to exceed current assets. We believe such a deficit has no significant impact on our liquidity or operations.

If our cash flows from operations are less than we require, we may need to access the capital markets to obtain financing. Our access to, and the availability of, financing on acceptable terms and conditions in the future or at all will be impacted by many factors, including, but not limited to:

- our financial performance;
- our credit ratings or absence of a credit rating;
- the liquidity of the overall capital markets; and
- the state of the Chinese, U.S. and global economies.

There can be no assurance, particularly as a new company that currently has no credit rating, that we will have access to the capital markets on terms acceptable to us or at all. See “Item 1A. Risk Factors” for a further discussion.

Generally our income is subject to the Chinese statutory tax rate of 25%. However, to the extent our cash flows from operations exceed our China cash requirements, the excess cash may be subject to an overall tax rate equal to the 35% U.S. statutory income tax rate.

Dividends and Share Repurchases

On February 7, 2017, we announced that our board of directors authorized a \$300 million share repurchase program. Yum China may repurchase shares under this program from time to time in open market or privately negotiated transactions, including block trades, accelerated share repurchase transactions and Rule 10b5-1 trading plans.

Our ability to declare and pay any dividends on our stock may be restricted by applicable Chinese laws. The laws, rules and regulations applicable to our Chinese subsidiaries permit payments of dividends only out of their accumulated profits, if any, determined in accordance with applicable Chinese accounting standards and regulations. Under Chinese law, an enterprise incorporated in China is required to set aside at least 10% of its after-tax profits each year, after making up previous years’ accumulated losses, if any, to fund certain statutory reserve funds, until the aggregate amount of such a fund reaches 50% of its registered capital. As a result, our Chinese subsidiaries are restricted in their ability to transfer a portion of their net assets to us in the form of dividends. At the discretion of the board of directors, as an enterprise incorporated in China, each of our Chinese subsidiaries may allocate a portion of its after-tax profits based on Chinese accounting standards to staff welfare and bonus funds. These reserve funds and staff welfare and bonus funds are not distributable as cash dividends.

Borrowing Capacity

As of December 31, 2016, the Company had credit facilities of RMB2,300 million (approximately \$330 million) in the aggregate.

The credit facilities have terms ranging from 1 to 3 years. Each credit facility bears interest based on the prevailing rate stipulated by the People's Bank of China and contains financial covenants including, among other things, limitations on certain additional indebtedness and liens, and certain other transactions specified in the respective agreement. Each credit facility contains a cross-default provision whereby our failure to make any payment on a principal amount from any credit facility will constitute a default on other credit facilities. Interest on any outstanding borrowings is due at least monthly. As of December 31, 2016, the full amount of borrowings were available to us under each facility.

Contractual Obligations

Our significant contractual obligations and payments as of December 31, 2016 included:

	Total	Less than 1 Year	1-3 Years	3-5 Years	More than 5 Years
Capital Leases ^(a)	\$ 45	\$ 3	\$ 6	\$ 6	\$ 30
Operating Leases ^(a)	3,048	444	796	668	1,140
Purchase Obligations ^(b)	319	319	—	—	—
Total Contractual Obligations	<u>\$ 3,412</u>	<u>\$ 766</u>	<u>\$ 802</u>	<u>\$ 674</u>	<u>\$ 1,170</u>

- (a) These obligations, which are shown on a nominal basis, relate primarily to more than 6,000 company-owned restaurants. See Note 12.
- (b) Purchase obligations include agreements to purchase goods or services that are enforceable and legally binding on us and that specify all significant terms, including: fixed or minimum quantities to be purchased; fixed, minimum or variable price provisions; and the approximate timing of the transaction. We have excluded agreements that are cancelable without penalty. Purchase obligations relate primarily to supply agreements.

We have not included in the contractual obligations table approximately \$31 million of liabilities for unrecognized tax benefits relating to various tax positions we have taken. These liabilities may increase or decrease over time as a result of tax examinations, and given the status of the examinations, we cannot reliably estimate the period of any cash settlement with the respective taxing authorities. These liabilities exclude amounts that are temporary in nature and for which we anticipate that over time there will be no net cash outflow.

Off-Balance Sheet Arrangements

See the Unconsolidated Affiliates Guarantees sections of Note 19 for discussion of our off-balance sheet arrangements.

Recently Adopted Accounting Pronouncements and New Accounting Pronouncements Not Yet Adopted

In May 2014, the Financial Accounting Standards Board (“FASB”) issued ASU No. 2014-09, Revenue from Contracts with Customers (Topic 606) (ASU 2014-09), to provide principles within a single framework for revenue recognition of transactions involving contracts with customers across all industries. In July 2015, the FASB approved a one-year deferral of the effective date of the new revenue standard. ASU 2014-09 is now effective for the Company in our first quarter of fiscal 2018 with early adoption permitted in the first quarter of 2017. The standard allows for either a full retrospective or modified retrospective transition method. In March and April 2016, the FASB issued the following amendments to clarify the implementation guidance: ASU No. 2016-08, Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations (Reporting Revenue Gross versus Net) and ASU No. 2016-10 Revenue from Contracts with Customers (Topic 606): Identifying Performance Obligations and Licensing. We do not believe these standards will impact our recognition of revenue from Company-owned restaurants or our recognition of continuing fees from franchisees, which are based on a percentage of franchise sales. However, the initial fees from franchisees, which are currently recognized as revenue when we have performed substantially all initial services required by the franchise agreement, generally upon the opening of a store, will be recognized over the term of the franchise agreement because the franchise rights will be accounted for as rights to access our symbolic intellectual property. Our initial fees, including renewal fees, of \$6 million were recognized as revenue during the year ended December 31, 2016. In addition, we are continuing to evaluate the impact the adoption of these standards will have on the recognition and presentation of other revenue transactions with unconsolidated affiliates and franchisees.

In July 2015, the FASB issued ASU No. 2015-11, Inventory (Topic 330) (ASU 2015-11), which requires inventory within the scope of the standard to be measured at the lower of cost and net realizable value. Net realizable value is defined as the estimated selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal, and transportation. ASU 2015-10 is effective for the Company in our first quarter of fiscal 2017 with early adoption permitted. We do not expect the adoption of this standard to have a material impact on our Consolidated and Combined Financial Statements.

In February 2016, the FASB issued ASU No. 2016-02, Leases (Topic 842) (ASU 2016-02), which increases transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. ASU 2016-02 is effective for the Company in our first quarter of fiscal 2019 with early adoption permitted. The standard must be adopted using a modified retrospective transition approach for leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements. We expect that this standard will have a material effect on our financial statements. While we are continuing to assess the effect of adoption, we currently believe the most significant changes relate to the recognition of right-of-use (“ROU”) assets and lease liabilities on our balance sheet for operating leases of the land and/or building of our restaurants and office space. At December 31, 2016, we operated more than 6,000 restaurants, leasing the underlying land and/or building, with our commitments expiring within 20 years from the inception of the lease. The amount of our future minimum lease payments under operating leases was approximately \$3 billion as of December 31, 2016. We anticipate continuing to add more restaurants and increase our leasing activity between now and adoption.

In March 2016, the FASB issued ASU No. 2016-09, Compensation-Stock Compensation (Topic 718) (ASU 2016-09): Improvements to Employee Share-Based Payment Accounting, which is intended to simplify several aspects of the accounting for employee share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. ASU 2016-09 is effective for the Company in our first quarter of fiscal 2017 with early adoption permitted. Upon adoption of this standard, excess tax benefits associated with share-based compensation, which are currently recognized within Common Stock, will be reflected within the income tax provision in our Consolidated and Combined Statements of Income. Additionally, our Consolidated and Combined Statements of Cash Flows will present such excess tax benefits, which are currently presented as a financing activity, as an operating activity. The impact of adopting this standard on our Consolidated and Combined Financial Statements will be dependent on the timing and intrinsic value of future share-based compensation award exercises.

In June 2016, the FASB issued ASU 2016-13, Financial Instruments-Credit Losses (Topic 326) (ASU 2016-13): Measurement of Credit Losses on Financial Instruments, which requires measurement and recognition of expected versus incurred credit losses for financial assets held. ASU 2016-13 is effective for the Company in our first quarter of fiscal 2020 with early adoption permitted beginning in the first quarter of fiscal 2019. We are currently evaluating the impact the adoption of this standard will have on our Consolidated and Combined Financial Statements.

In August 2016, the FASB issued ASU 2016-15, Statement of Cash Flows (Topic 230) (ASU 2016-15), which provides clarification regarding how certain cash receipts and cash payment are presented and classified in the statement of cash flows. This update addresses eight specific cash flow issues with the objective of reducing the existing diversity in practice. ASU 2016-15 is effective for annual and interim periods beginning after December 15, 2017, which will require us to adopt these provisions in the first quarter of fiscal 2018 using a retrospective transition method with early adoption is permitted. We are currently evaluating the impact the adoption of this standard will have on our Consolidated and Combined Financial Statements.

Critical Accounting Policies and Estimates

Our reported results are impacted by the application of certain accounting policies that require us to make subjective or complex judgments. These judgments involve estimations of the effect of matters that are inherently uncertain and may significantly impact our quarterly or annual results of operations or financial condition. Changes in the estimates and judgments could significantly affect our results of operations, financial condition and cash flows in future years. A description of what we consider to be our most significant critical accounting policies follows.

Impairment or Disposal of Long-Lived Assets

We review long-lived assets of restaurants (primarily PP&E and allocated intangible assets subject to amortization) semi-annually for impairment, or whenever events or changes in circumstances indicate that the carrying amount of a restaurant may not be recoverable. We evaluate recoverability based on the restaurant's forecasted undiscounted cash flows, which incorporate our best estimate of sales growth and margin improvement based upon our plans for the unit and actual results at comparable restaurants. Our restaurant impairment indicator and recoverability tests do not include a deduction for license fees paid to YUM before our separation on October 31, 2016. However such license fee paid to YUM is included in the impairment indicator and recoverability tests after the separation, as our relationship with YUM changed from one between subsidiary and parent prior to the separation to the one between the licensee and a third-party licensor after the separation. As a result of including the license fees paid to YUM, the additional impairment assessment performed as of November 1, 2016 resulted in incremental restaurant-level impairment of \$17 million. For restaurant assets that are deemed not to be recoverable, we write down the impaired restaurant to its estimated fair value. Key assumptions in the determination of fair value are the future after-tax cash flows of the restaurant, which are reduced by future royalties a franchisee would pay, and a discount rate. The after-tax cash flows incorporate reasonable sales growth and margin improvement assumptions that would be used by a franchisee in the determination of a purchase price for the restaurant. Estimates of future cash flows are highly subjective judgments and can be significantly impacted by changes in the business or economic conditions.

When we believe it is more likely than not a restaurant or groups of restaurants will be refranchised for a price less than their carrying value, but do not believe the restaurant(s) have met the criteria to be classified as held for sale, we review the restaurants for impairment. Expected net sales proceeds are generally based on actual bids from the buyer, if available, or anticipated bids given the discounted projected after-tax cash flows for the group of restaurants. Historically, these anticipated bids have been reasonably accurate estimations of the proceeds ultimately received. The after-tax cash flows used in determining the anticipated bids incorporate reasonable assumptions we believe a franchisee would make such as sales growth and margin improvement as well as expectations as to the useful lives of the restaurant assets. These after-tax cash flows also include a deduction for the anticipated, future royalties we would receive under a franchise agreement with terms substantially at market entered into simultaneously with the refranchising transaction.

The discount rate used in the fair value calculations is our estimate of the required rate of return that a franchisee would expect to receive when purchasing a similar restaurant or groups of restaurants and the related long-lived assets. The discount rate incorporates rates of returns for historical refranchising market transactions and is commensurate with the risks and uncertainty inherent in the forecasted cash flows.

We evaluate indefinite-lived intangible assets for impairment on an annual basis or more often if an event occurs or circumstances change that indicates impairment might exist. We perform our annual test for impairment of our indefinite-lived intangible assets at the beginning of our fourth quarter. Fair value is an estimate of the price a willing buyer would pay for the intangible asset and is generally estimated by discounting the expected future after-tax cash flows associated with the intangible asset. Our only indefinite-lived intangible asset is our Little Sheep trademark. In 2014, we recorded impairment charges of \$284 million to write the Little Sheep trademark down to its estimated fair value. The Little Sheep trademark has a book value of \$53 million at December 31, 2016. Our 2016 and 2015 fair value estimate of the Little Sheep trademark exceeded its carrying value. Fair value was determined using a relief-from-royalty valuation approach that included estimated future revenues as a significant input, and a discount rate of 12% and 13% for 2016 and 2015, respectively, as our estimate of the required rate-of-return that a third-party buyer would expect to receive when purchasing the Little Sheep trademark. The primary drivers of fair value include franchise revenue growth and revenues from a wholly-owned business that sells seasoning to retail customers. Franchise revenue growth reflects annual same-store sales growth of 4% and approximately 35 new franchise units per year, partially offset by the impact of approximately 25 franchise closures per year. The seasoning business is forecasted to generate sales growth rates consistent with historical results.

Impairment of Goodwill

We evaluate goodwill for impairment on an annual basis as of the beginning of our fourth quarter or more often if an event occurs or circumstances change that indicates impairment might exist. Goodwill is evaluated for impairment by determining whether the fair value of our reporting units exceed their carrying values. Our reporting units are our individual operating segments. Fair value is the price a willing buyer would pay for the reporting unit, and is generally estimated using discounted expected future after-tax cash flows from Company-owned restaurant operations and franchise royalties.

Future cash flow estimates and the discount rate are the key assumptions when estimating the fair value of a reporting unit. Future cash flows are based on growth expectations relative to recent historical performance and incorporate sales growth and margin improvement assumptions that we believe a third-party buyer would assume when determining a purchase price for the reporting unit. The sales growth and margin improvement assumptions that factor into the discounted cash flows are highly correlated as cash flow growth can be achieved through various interrelated strategies such as product pricing and restaurant productivity initiatives. The discount rate is our estimate of the required rate of return that a third-party buyer would expect to receive when purchasing a business from us that constitutes a reporting unit. We believe the discount rate is commensurate with the risks and uncertainty inherent in the forecasted cash flows.

Other than the Little Sheep reporting unit discussed below, the fair values of our other reporting units were substantially in excess of their respective carrying values as of the goodwill testing dates in 2016, 2015 and 2014, respectively.

In 2014, we completely impaired the remaining goodwill balance at the Little Sheep reporting unit of \$160 million. The fair value of the Little Sheep reporting unit was based on the estimated price a willing buyer would pay, and was determined using an income approach with future cash flow estimates generated by the business as a significant input. Future cash flow estimates were impacted by assumptions related to new unit development, sales growth and margin improvement. These fair values incorporated a discount rate of 13% as our estimate of the required rate of return that a third-party buyer would expect to receive when purchasing the Little Sheep reporting unit.

When we rebrand restaurants, we include goodwill in the carrying amount of the restaurants disposed of based on the relative fair values of the portion of the reporting unit disposed of in the rebranding versus the portion of the reporting unit that will be retained. The fair value of the portion of the reporting unit disposed of in a rebranding is determined by reference to the discounted value of the future cash flows expected to be generated by the restaurant and retained by the franchisee, which include a deduction for the anticipated, future royalties the franchisee will pay us associated with the franchise agreement entered into simultaneously with the rebranding transaction. Appropriate adjustments are made to the fair value determinations if such franchise agreement is determined to not be at prevailing market rates.

The discounted value of the future cash flows expected to be generated by the restaurant and retained by the franchisee is reduced by future royalties the franchisee will pay the Company. The Company thus considers the fair value of future royalties to be received under the franchise agreement as fair value retained in its determination of the goodwill to be written off when rebranding. Others may consider the fair value of these future royalties as fair value disposed of and thus would conclude that a larger percentage of a reporting unit's fair value is disposed of in a rebranding transaction.

Financial Instruments

The Post-Closing Adjustment related to and the warrants issued in the investment with the Investors are accounted for as derivative instruments and liability-classified equity contracts, respectively (see Note 11). They were initially measured at fair value as of November 1, 2016, the date when shares of common stock were issued, and were subject to subsequent fair value measurement until December 30, 2016. The Company adopted the Monte-Carlo Simulation model and the Black-Scholes option-pricing model in deriving the fair value of the Post-Closing Adjustment and the warrants, respectively.

Under the valuation models, we made a number of assumptions, including:

- the expected future volatility of the price of shares of Yum China common stock;
- the risk-free interest rate;
- the expected dividend yield; and
- the estimated price of shares of Yum China common stock over the measurement period.

We estimated the expected future volatility of Yum China common stock based on the historical price volatility of the publicly traded shares of common stock of comparable companies. The risk-free interest rate was based on the U.S. Treasury zero-coupon yield in effect with maturity terms equal to the term of the financial instruments. The dividend yield was estimated to be zero. The estimated price of shares of Yum China common stock over the measurement period was based on simulated stock prices and the market conditions defined in the terms in each simulated path.

The valuation models require the input of highly subjective assumptions. Changes in the subjective input assumptions can materially affect the fair value estimate and, as a result, our operating income and net income.

Share-Based Compensation

We account for share awards issued to employees in accordance with Accounting Standards Codification (“ASC”) Topic 718 (“ASC 718”), *Compensation-Stock Compensation*. Share-based compensation cost is measured at the grant date based on the fair value of the award and is recognized as an expense, net of estimated forfeitures, over the requisite service period, which is generally the vesting period. We recognize share-based compensation expense for awards granted to employees and non-employee directors using the straight-line method.

We estimated the fair value of our share-based awards at the grant date using the Black Scholes option-pricing model. It should be noted that the option pricing model requires the input of highly subjective assumptions. Changes in the subjective input assumptions can materially affect the fair value estimate and, as a result, our operating income and net income.

Under the Black Scholes option-pricing model, we made a number of assumptions regarding the fair value of the share-based awards, including:

- the expected future volatility of the price of shares of Yum China common stock;
- the risk-free interest rate;

- the expected dividend yield; and
- the expected term.

We estimated the expected future volatility of the price of shares of Yum China common stock based on the historical price volatility of the publicly traded shares of common stock of comparable companies. The risk-free interest rate was based on the U.S. Treasury zero-coupon yield in effect with maturity terms equal to the expected term of the awards. The dividend yield was estimated to be zero. We use historical turnover data to estimate the expected forfeiture rate.

PRC Value-Added Tax

At each balance sheet date, the Company reviews the outstanding balance of any net VAT credit asset for recoverability assessment. We evaluate the recoverability of the net VAT credit asset based on our estimated operating results and capital spending, which inherently include significant assumptions subject to change. Key assumptions include the following:

- Estimated growth rate for revenues;
- Estimated restaurant expenses and other costs;
- Estimated new unit development and asset upgrades.

We also consider qualitative factors including the fact that such assets can be carried forward indefinitely to offset future net VAT payables, our ability to manage the accumulation of the input VAT credits and potential changes in VAT rates. Changes in any of the assumptions could materially impact the amount of net VAT asset and its recoverability and, as a result, our operating income and net income.

Income Taxes

Prior to October 31, 2016, our operations have historically been included in the U.S. federal and U.S. state income tax returns filed by YUM. Our foreign income tax returns, primarily those filed by our China subsidiaries, are filed on an individual entity basis. Income tax expense and other income tax related information contained in our Consolidated and Combined Financial Statements are presented on a separate return basis as if we filed our own U.S. federal and U.S. state tax returns rather than having been included in these YUM tax returns. The separate return method applies the accounting guidance for income taxes to the standalone financial statements as if we were a separate taxpayer and a standalone enterprise for the periods presented prior to October 31, 2016. The calculation of our income taxes on a separate return basis requires a considerable amount of judgment and the use of both estimates and allocations. Current income tax liabilities related to our operations under the separate return method as of October 31, 2016 are assumed to be immediately settled with YUM and are relieved through the Parent Company Investment account and the net transfers to parent in the Consolidated and Combined Statements of Cash Flows. Subsequent to October 31, 2016, the Company became a separate taxpayer and will prepare its own consolidated U.S. federal income tax return and U.S. state income tax filings.

At December 31, 2016 and 2015, we had valuation allowances of approximately \$41 million and \$45 million to reduce our \$209 million and \$173 million of deferred tax assets, respectively, to amounts that are more likely than not to be realized. The deferred tax assets not subject to a valuation allowance primarily relate to temporary differences in our profitable China legal entities. In evaluating our ability to recover our deferred tax assets, we consider future taxable income as well as carryforward periods and restrictions on usage. The estimation of future taxable income and our resulting ability to utilize deferred tax assets can significantly change based on future events, including our determinations as to feasibility of certain tax planning strategies. Thus, recorded valuation allowances may be subject to material future changes.

As a matter of course, we are regularly subject to tax audits and examination by federal, state and foreign tax authorities. We recognize the benefit of positions taken or expected to be taken in our tax returns when it is more likely than not that the position would be sustained upon examination by these tax authorities. A recognized tax position is then measured at the largest amount of benefit that is greater than fifty percent likely of being realized upon settlement. At December 31, 2016 and 2015 we had \$26 million and \$15 million, respectively, of unrecognized tax benefits. We evaluate unrecognized tax benefits, including interest thereon, on a quarterly basis to ensure that they have been appropriately adjusted for events, including audit settlements, which may impact our ultimate payment for such exposures.

We have investments in foreign subsidiaries where the carrying values for financial reporting exceed the tax basis. We have not provided deferred tax on the portion of the excess that we believe is indefinitely reinvested, as we have the ability and intent to indefinitely postpone these basis differences from reversing with a tax consequence. We estimate that our total temporary difference upon which we have not provided deferred tax is approximately \$1.5 billion at December 31, 2016. However, it is not practicable to determine the deferred tax liability on this amount due to uncertainty with regard to the timing or manner of repatriation and the related impact on local taxes, withholding taxes and foreign tax credits.

If our intentions regarding our ability and intent to postpone these basis differences from reversing with a tax consequence change, deferred tax liability may need to be provided on this excess that could materially impact the provision for income taxes.

See Note 17 of the Consolidated and Combined Financial Statements for a further discussion of our income taxes.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk.

Quantitative and Qualitative Disclosures About Market Risk

Foreign Currency Exchange Rate Risk

Changes in foreign currency exchange rates impact the translation of our reported foreign currency denominated earnings, cash flows and net investments in foreign operations, virtually all of which are denominated in RMB. We chose not to hedge our foreign currency denominated earnings through the use of financial instruments, and attempted to minimize the related exposure by purchasing goods and services from third parties in local currencies when practical.

As substantially all of the Company's assets are located in China, the Company is exposed to movements in the RMB foreign currency exchange rate. For the year ended December 31, 2016, the Company's Operating Profit would have decreased approximately \$82 million if the RMB weakened 10% relative to the U.S. dollar. This estimated reduction assumes no changes in sales volumes or local currency sales or input prices.

Commodity Price Risk

We are subject to volatility in food costs as a result of market risk associated with commodity prices. Our ability to recover increased costs through higher pricing is, at times, limited by the competitive environment in which we operate. We manage our exposure to this risk primarily through pricing agreements with our vendors.

Item 8. Financial Statements and Supplementary Data.

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Financial Statement Schedules

No schedules are required because either the required information is not present or not present in amounts sufficient to require submission of the schedule, or because the information required is included in the above-listed financial statements or notes thereto.

Report of Independent Registered Public Accounting Firm

The Board of Directors and Shareholders
YUM China Holdings, Inc.:

We have audited the accompanying consolidated and combined balance sheets of YUM China Holdings, Inc. and subsidiaries (the “Company”) as of December 31, 2016 and 2015, and the related consolidated and combined statements of income (loss), comprehensive income (loss), equity, and cash flows for each of the years in the three-year period ended December 31, 2016. These consolidated and combined financial statements are the responsibility of the Company’s management. Our responsibility is to express an opinion on these consolidated and combined financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated and combined financial statements referred to above present fairly, in all material respects, the financial position of Yum China Holdings Inc. and subsidiaries as of December 31, 2016 and 2015, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2016, in conformity with U.S. generally accepted accounting principles.

As discussed in Note 1 and Note 2, the combined financial statements, constituting the periods prior to October 31, 2016, include Yum! Brands, Inc.’s (“YUM”) China businesses and operations and have been derived from the consolidated financial statements and underlying accounting records of YUM. The combined financial statements also include expense allocations for certain corporate functions historically provided by YUM. These allocations may not be reflective of the actual expense which would have been incurred had the Company operated as a separate entity apart from YUM prior to October 31, 2016.

/s/ KPMG Huazhen LLP
Shanghai, China
March 8, 2017

Consolidated and Combined Statements of Income (Loss)

Yum China Holdings, Inc.

Years ended December 31, 2016, 2015 and 2014

(in US\$ millions, except for per share data)

	2016	2015	2014
Revenues			
Company sales	\$ 6,622	\$ 6,789	\$ 6,821
Franchise fees and income	130	120	113
Total revenues	<u>6,752</u>	<u>6,909</u>	<u>6,934</u>
Costs and Expenses, Net			
Company restaurants			
Food and paper	1,919	2,159	2,207
Payroll and employee benefits	1,432	1,386	1,407
Occupancy and other operating expenses	2,259	2,386	2,415
Company restaurant expenses	<u>5,610</u>	<u>5,931</u>	<u>6,029</u>
General and administrative expenses	424	395	389
Franchise expenses	71	70	64
Closures and impairment expenses, net	78	64	517
Refranchising gain, net	(15)	(13)	(17)
Other income, net	(56)	(26)	(51)
Total costs and expenses, net	<u>6,112</u>	<u>6,421</u>	<u>6,931</u>
Operating Profit	640	488	3
Interest income, net	11	8	14
Changes in fair value of financial instruments	21	—	—
Income Before Income Taxes	672	496	17
Income tax provision	(158)	(168)	(54)
Net income (loss) – including noncontrolling interests	514	328	(37)
Net income (loss) – noncontrolling interests	12	5	(30)
Net Income (Loss) – Yum China Holdings, Inc.	<u>\$ 502</u>	<u>\$ 323</u>	<u>\$ (7)</u>
Basic Earnings (Loss) Per Common Share	<u>\$ 1.36</u>	<u>\$ 0.89</u>	<u>\$ (0.02)</u>
Diluted Earnings (Loss) Per Common Share	<u>\$ 1.36</u>	<u>\$ 0.89</u>	<u>\$ (0.02)</u>

See accompanying Notes to Consolidated and Combined Financial Statements.

Consolidated and Combined Statements of Comprehensive Income (Loss)

Yum China Holdings, Inc.

Years ended December 31, 2016, 2015 and 2014

(in US\$ millions)

	2016	2015	2014
Net income (loss) - including noncontrolling interests	\$ 514	\$ 328	\$ (37)
Other comprehensive income (loss), net of tax of nil			
Foreign currency losses arising during the year	(132)	(93)	(52)
Comprehensive income (loss) - including noncontrolling interests	382	235	(89)
Comprehensive income (loss) - noncontrolling interests	9	(1)	(32)
Comprehensive Income (Loss) - Yum China Holdings, Inc.	\$ 373	\$ 236	\$ (57)

See accompanying Notes to Consolidated and Combined Financial Statements.

Consolidated and Combined Statements of Cash Flows

Yum China Holdings, Inc.

Years ended December 31, 2016, 2015 and 2014

(in US\$ millions)

	2016	2015	2014
Cash Flows – Operating Activities			
Net income (loss) – including noncontrolling interests	\$ 514	\$ 328	\$ (37)
Depreciation and amortization	402	425	411
Closures and impairment expenses	78	64	517
Refranchising gain	(15)	(13)	(17)
Deferred income taxes	(40)	29	(104)
Equity income from investments in unconsolidated affiliates	(54)	(41)	(30)
Distributions of income received from unconsolidated affiliates	35	21	28
Excess tax benefit from share-based compensation	(2)	(3)	(2)
Share-based compensation expense	16	14	13
Changes in fair value of financial instruments	(21)	—	—
Changes in accounts receivable	(54)	(5)	(5)
Changes in inventories	(96)	61	(21)
Changes in prepaid expenses and other current assets	7	(8)	21
Changes in accounts payable and other current liabilities	123	31	39
Changes in income taxes payable	6	(14)	(44)
Other, net	(35)	21	6
Net Cash Provided by Operating Activities	864	910	775
Cash Flows – Investing Activities			
Capital spending	(436)	(512)	(525)
Purchases of short-term investments	(136)	(40)	(427)
Maturities of short-term investments	53	40	427
Proceeds from refranchising of restaurants	32	27	31
Proceeds from disposal of aircraft	19	—	—
Other, net	(3)	(8)	(18)
Net Cash Used in Investing Activities	(471)	(493)	(512)
Cash Flows – Financing Activities			
Net transfers to Parent	(357)	(214)	(316)
Payment of capital lease obligations	(3)	(2)	(1)
Short-term borrowings, by original maturity			
More than three months – proceeds	—	—	2
More than three months – payments	—	—	(2)
Excess tax benefit from share-based compensation	2	3	2
Proceeds from issuance of common stock and warrants	460	—	—
Other, net	(7)	—	(4)
Net Cash Provided by (Used in) Financing Activities	95	(213)	(319)
Effect of Exchange Rates on Cash and Cash Equivalents	(28)	(17)	(6)
Net Increase (Decrease) in Cash and Cash Equivalents	460	187	(62)
Cash and Cash Equivalents – Beginning of Year	425	238	300
Cash and Cash Equivalents – End of Year	\$ 885	\$ 425	\$ 238
Supplemental Cash Flow Data			
Cash paid for income tax	182	143	186

See accompanying Notes to Consolidated and Combined Financial Statements.

Consolidated and Combined Balance Sheets

Yum China Holdings, Inc.

December 31, 2016 and 2015

(in US\$ millions, except for number of shares)

	2016	2015
ASSETS		
Current Assets		
Cash and cash equivalents	\$ 885	\$ 425
Short-term investments	79	—
Accounts receivable, net	74	33
Inventories, net	268	189
Prepaid expenses and other current assets	120	152
Total Current Assets	\$ 1,426	\$ 799
Property, plant and equipment, net	1,647	1,841
Goodwill	79	85
Intangible assets, net	88	107
Investments in unconsolidated affiliates	71	61
Other assets	254	192
Deferred income taxes	162	116
Total Assets	\$ 3,727	\$ 3,201
LIABILITIES, REDEEMABLE NONCONTROLLING INTEREST AND EQUITY		
Current Liabilities		
Accounts payable and other current liabilities	\$ 971	\$ 926
Income taxes payable	33	22
Total Current Liabilities	1,004	948
Capital lease obligations	28	34
Other liabilities and deferred credits	252	234
Total Liabilities	1,284	1,216
Redeemable Noncontrolling Interest	—	6
Equity		
Common stock, \$0.01 par value; 1,000,000,000 shares authorized; 383,344,835.42 shares issued and outstanding at December 31, 2016	4	—
Treasury stock	(20)	—
Additional paid-in capital	2,352	—
Retained earnings ^(a)	40	—
Parent Company Investment ^(b)	—	1,791
Accumulated other comprehensive income	1	130
Total Equity – Yum China Holdings, Inc.	2,377	1,921
Noncontrolling interests	66	58
Total Equity	2,443	1,979
Total Liabilities, Redeemable Noncontrolling Interest and Equity	\$ 3,727	\$ 3,201

(a) Retained earnings represent the Company's earnings after taxes generated from November 1, 2016 to December 31, 2016.

(b) Parent Company Investment represents YUM's historical investment in the Company, the Company's accumulated net earnings after taxes, and the net effect of transactions with and allocations from YUM. Upon the separation, Parent Company Investment was reclassified into the Company's common stock and additional paid-in capital.

See accompanying Notes to Consolidated and Combined Financial Statements.

Consolidated and Combined Statements of Equity

Yum China Holdings, Inc.

Years ended December 31, 2016, 2015 and 2014

(in US\$ millions, except for number of shares)

	Yum China Holdings, Inc.											
	Common Stock		Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income	Parent Company Investment	Treasury Stock		Noncontrolling Interests	Total Equity	Redeemable Noncontrolling Interest	
	Shares	Amount					Shares	Amount				
Balance at												
December 31, 2013		— \$	— \$	— \$	— \$	267 \$	2,014	— \$	— \$	63	\$2,344 \$	39
Net loss							(7)			(1)	(8)	(29)
Foreign currency translation losses					(50)					(1)	(51)	(1)
Comprehensive loss											(59)	(30)
Dividends declared										(4)	(4)	—
Net transfers to Parent							(336)				(336)	
Balance at												
December 31, 2014		— \$	— \$	— \$	— \$	217 \$	1,671	— \$	— \$	57	\$1,945 \$	9
Net Income (loss)							323			6	329	(1)
Foreign currency translation losses					(87)					(4)	(91)	(2)
Comprehensive income (loss)											238	(3)
Acquisition of Little Sheep store-level noncontrolling interests							1			(1)	—	
Net transfers to Parent							(204)				(204)	
Balance at												
December 31, 2015		— \$	— \$	— \$	— \$	130 \$	1,791	— \$	— \$	58	\$1,979 \$	6
Net Income				40			462			19	521	1
Noncontrolling interest loss upon redemption											—	(8)
Foreign currency translation gains (losses)					(129)					(4)	(133)	1
Comprehensive income (loss)											388	(6)
Dividends declared										(7)	(7)	
Net transfers to Parent							(360)				(360)	
Capitalization at separation	363,758,219.00		4	1,889			(1,893)				—	
Issuance of common stock to Investors	19,145,169.42			364							364	
Reclassification of warrants issued to Investors				95							95	
Stock repurchased from Investors ^(a)							(784,686.42)	(20)			(20)	
Exercise and vesting of share-based awards	441,447.00										—	
Share-based compensation				4							4	
Balance at												
December 31, 2016	383,344,835.42	\$	4 \$	2,352 \$	40 \$	1 \$	—	(784,686.42) \$	(20) \$	66	\$2,443 \$	—

(a) Pursuant to the investment agreement with the Investors, 19,145,169.42 shares issued on November 1, 2016 were subject to Post-Closing Adjustment on December 30, 2016, and 784,686.42 shares were subsequently repurchased on January 9, 2017. The repurchased shares were treated as treasury stock as of December 31, 2016. See Note 11.

See accompanying Notes to Consolidated and Combined Financial Statements.

Notes to Consolidated and Combined Financial Statements

(Tabular amounts in US\$ millions, except for number of shares and per share data)

Note 1 – Description of Business

Yum China Holdings, Inc. (“Yum China” and, together with its subsidiaries, the “Company,” “we,” “us,” and “our”) was incorporated in Delaware on April 1, 2016. The Company separated from Yum! Brands, Inc. (“YUM” or the “Parent”) on October 31, 2016 (the “separation”), becoming an independent publicly traded company as a result of a pro rata distribution (the “distribution”) of all outstanding shares of Yum China common stock to shareholders of YUM. On October 31, 2016, YUM’s shareholders of record as of 5:00 p.m. Eastern Time on October 19, 2016 received one share of Yum China common stock for every one share of YUM common stock held as of the record date. Yum China’s common stock began trading “regular way” under the ticker symbol “YUMC” on the New York Stock Exchange on November 1, 2016.

The Company owns, franchises or has ownership in entities that own and operate restaurants under the KFC, Pizza Hut Casual Dining, Pizza Hut Home Service, Taco Bell, East Dawning and Little Sheep concepts (collectively, the “Concepts”). In connection with the separation of the Company from YUM, Yum! Restaurants Asia Pte. Ltd., a wholly-owned indirect subsidiary of YUM, and Yum Restaurants Consulting (Shanghai) Company Limited (“YCCL”), a wholly-owned indirect subsidiary of the Company, entered into a 50-year master license agreement with automatic renewals for additional consecutive renewal terms of 50 years each, subject only to YCCL being in “good standing” and unless YCCL gives notice of its intent not to renew, for the exclusive right to use and sublicense the use of intellectual property owned by YUM and its subsidiaries for the development and operation of the KFC, Pizza Hut and, subject to achieving certain agreed upon milestones, Taco Bell brands and their related marks and other intellectual property rights for restaurant services in the People’s Republic of China (the “PRC” or “China”), excluding Hong Kong, Taiwan and Macau. In exchange, we pay a license fee to YUM equal to 3% of net system sales from both our Company and franchise restaurants. We own the East Dawning and Little Sheep intellectual property and pay no license fee related to these concepts.

The operations of each Concept represent an operating segment of the Company within these Consolidated and Combined Financial Statements. We have two reportable segments: KFC and Pizza Hut Casual Dining. Our remaining operating segments, including the operations of Pizza Hut Home Service, East Dawning, Little Sheep and Taco Bell, are combined and referred to as All Other Segments, as those operating segments are insignificant both individually and in the aggregate.

In 1987, KFC was the first quick-service restaurant brand to enter China. As of December 31, 2016, there are over 5,200 KFCs in China. We maintain a 58% and 70% controlling interest in the entities that own and operate the KFCs in Shanghai and Beijing, respectively. We have a 47% noncontrolling ownership in each of our unconsolidated affiliates that own and operate KFCs in Hangzhou, Suzhou and Wuxi.

<u>KFC Unit Count</u>	2016	2015	2014
Company - owned	3,913	3,821	3,732
Unconsolidated affiliates	836	796	757
Franchise	475	386	339
	<u>5,224</u>	<u>5,003</u>	<u>4,828</u>

The first Pizza Hut Casual Dining in China opened in 1990. As of December 31, 2016, there are over 1,700 Pizza Hut Casual Dining restaurants in China.

<u>Pizza Hut Casual Dining Unit Count</u>	2016	2015	2014
Company - owned	1,690	1,556	1,310
Franchise	24	16	3
	<u>1,714</u>	<u>1,572</u>	<u>1,313</u>

Note 2 – Summary of Significant Accounting Policies

In connection with our separation from YUM, the direct and indirect equity interests of all of our operating subsidiaries and intermediate holding companies were transferred from YUM to Yum China, when Yum China was still one of YUM’s subsidiaries, through a series of transactions, which were completed in August 2016. The Company separated from YUM on October 31, 2016, becoming an independent publicly traded company as a result of a pro rata distribution of all outstanding shares of Yum China common stock to shareholders of YUM.

The financial statements presented herein represent (i) prior to October 31, 2016, the Combined Financial Statements of YUM’s China businesses and operations when the Company was a wholly owned subsidiary of YUM and (ii) subsequent to October 31, 2016, the Consolidated Financial Statements of the Company as a separate publicly traded company following its separation from YUM.

Our preparation of the accompanying Consolidated and Combined Financial Statements in conformity with Generally Accepted Accounting Principles in the United States of America (“GAAP”) requires us to make estimates and assumptions that affect reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

Basis of Preparation and Principles of Consolidation. The accompanying Combined Financial Statements have been prepared on a standalone basis and are derived from YUM’s consolidated financial statements and underlying accounting records. Transactions between the Company and YUM that were not cash settled were considered to be effectively settled at the time the transactions are recorded. The Combined Financial Statements include all revenues, costs, assets and liabilities directly attributable to the Company either through specific identification or allocation. The Consolidated and Combined Statements of Income (Loss) include allocations for certain of YUM’s Corporate functions which provided a direct benefit to the Company. These costs have been allocated based on Company system sales relative to YUM’s global system sales. System sales includes the sales results of all restaurants regardless of ownership. All allocated costs have been deemed to have been paid to YUM in the period in which the costs were recorded. The Company considers the cost allocation methodology and results to be reasonable for the periods prior to October 31, 2016. However, the allocations may not be indicative of the actual expense that would have been incurred had the Company operated as an independent, publicly traded company for the periods prior to October 31, 2016. Upon the separation, Parent Company Investment was adjusted as a result of settlement of certain assets and liabilities with YUM and formed the Company’s common stock and additional paid-in capital. See Note 3 for further discussion.

Intercompany accounts and transactions have been eliminated in consolidation. We consolidate entities in which we have a controlling financial interest, the usual condition of which is ownership of a majority voting interest. We also consider for consolidation an entity, in which we have certain interests, where the controlling financial interest may be achieved through arrangements that do not involve voting interests. Such an entity, known as a variable interest entity (“VIE”), is required to be consolidated by its primary beneficiary. The primary beneficiary is the entity that possesses the power to direct the activities of the VIE that most significantly impact its economic performance and has the obligation to absorb losses or the right to receive benefits from the VIE that are significant to it.

Our most significant variable interests are in entities that operate restaurants under franchise arrangements. We do not generally have an equity interest in our franchisee businesses with the exception of certain entities discussed below. Additionally, we do not typically provide significant financial support such as loans or guarantees to our franchisees. We have variable interests in certain entities that operate restaurants under franchise agreements through real estate lease arrangements with them to which we are a party. At December 31, 2016, the Company had future lease payments due from franchisees, on a nominal basis, of approximately \$95 million. As our franchise arrangements provide our franchisee entities the power to direct the activities that most significantly impact their economic performance, we do not consider ourselves the primary beneficiary of any such entity that might otherwise be considered a VIE.

We consolidate the entities that operate KFCs in Shanghai and Beijing where we have controlling interests of 58% and 70%, respectively. We report Net income (loss) attributable to noncontrolling interests, which includes the minority shareholders of the entities separately on the face of our Consolidated and Combined Statements of Income. The portion of equity not attributable to the Company for these entities is reported within equity, separately from the Company's equity on the Consolidated and Combined Balance Sheets.

We have a noncontrolling 47% interest in each of the entities that operate the KFCs in Hangzhou, Suzhou and Wuxi. We account for these entities by the equity method. These entities are not VIEs and our lack of majority voting rights precludes us from controlling these affiliates. Thus, we do not consolidate these affiliates. Instead, we account for them under the equity method. Our share of the net income or loss of these unconsolidated affiliates is included in Other income, net.

At December 31, 2015, the founding shareholders that owned the remaining 7% ownership interest in Little Sheep held an option that, if exercised, requires us to redeem their noncontrolling interest. This redeemable noncontrolling interest was classified outside permanent equity and recorded in the Consolidated and Combined Balance Sheets at the greater of the initial carrying amount adjusted for the noncontrolling interest's share of net income (loss), or its redemption value, as of December 31, 2015. During the year ended December 31, 2016, the Little Sheep founding shareholders sold their remaining 7% Little Sheep ownership interest to us pursuant to their redemption rights.

Comparative Information. Certain comparative items in the Consolidated and Combined Financial Statements have been reclassified to conform to the current year's presentation to facilitate comparison.

Fiscal Calendar. Our fiscal year ends on December 31. The Company operates on a fiscal monthly calendar, with two months in the first quarter, three months in the second and third quarters and four months in the fourth quarter.

Foreign Currency. Our functional currency for the operating entities in China is the Chinese Renminbi ("RMB"), the currency of the primary economic environment in which they operate. Income and expense accounts for our operations are then translated into U.S. dollars at the average exchange rates prevailing during the period. Assets and liabilities are then translated into U.S. dollars at exchange rates in effect at the balance sheet date. As of December 31, 2016, net cumulative translation adjustment gains of \$1 million were recorded in Accumulated other comprehensive income in the Consolidated and Combined Balance Sheets. Gains and losses arising from the impact of foreign currency exchange rate fluctuations on transactions in foreign currency, to the extent they arise, are included in Other income, net in our Consolidated and Combined Statements of Income.

Franchise Operations. We execute agreements which set out the terms of our arrangement with franchisees. Our franchise agreements typically require the franchisee to pay an initial, non-refundable fee and continuing fees based upon a percentage of sales. Subject to our approval and their payment of a renewal fee, a franchisee may generally renew the franchise agreement upon its expiration.

The internal costs we incur to provide support services to our franchisees are charged to General and Administrative (“G&A”) expenses as incurred. Certain direct costs of our franchise operations are charged to Franchise expenses. These costs include provisions for estimated uncollectible fees, rent or depreciation expense associated with restaurants we sublease to franchisees, and certain other direct incremental franchise support costs. The 3% license fee we pay to YUM for the right to sublicense the KFC, Pizza Hut and Taco Bell intellectual property is also recorded in Franchise expenses.

License fees due to YUM for our Company-owned stores are included within restaurant margin in Occupancy and other operating expenses in the Consolidated and Combined Statements of Income. License fees due to YUM on franchise sales are included in Franchise Expenses. Total license fees paid to YUM were \$249 million, \$269 million and \$265 million during the years ended December 31, 2016, 2015 and 2014.

Revenue Recognition. Revenues from Company-owned restaurants are recognized when payment is tendered at the time of sale. The Company presents sales net of sales-related taxes. The license fee we pay to YUM as a percentage of these Company sales is included in Occupancy and other operating expenses. We recognize income from gift cards when the gift card is redeemed by the customer. We recognize breakage revenue, which is the amount of gift card proceeds that is not expected to be redeemed, when the likelihood of redemption becomes remote.

Income from our franchisees includes initial fees, continuing fees, renewal fees and rental income from restaurants we sublease to them. We recognize initial fees received from a franchisee as revenue when we have performed substantially all initial services required by the franchise agreement, which is generally upon the opening of a store. We recognize continuing fees, which are based upon a percentage of franchisee sales, as those sales occur and rental income is recognized as it is earned. We recognize renewal fees when a renewal agreement with a franchisee becomes effective. We present initial fees collected upon the sale of a Company-owned restaurant to a franchisee in Refranchising gain, net.

Customer Loyalty Program. The Company’s KFC reportable segment operates a customer loyalty program which allows registered members to earn points for each qualifying purchase. Points, which generally expire 18 months after being earned, enable members to receive a coupon that may be redeemed primarily against future purchases of the KFC’s branded products for free or at a discounted price. Points cannot be redeemed for cash. The retail value of points earned by the loyalty program members is recorded as a reduction of revenue at the time the points are earned, based on the percentage of points that are projected to be redeemed, with a corresponding deferred revenue liability included in Accounts payable and other current liabilities in the Consolidated and Combined Balance Sheets. The Company recognizes the deferred revenue as revenue when (i) a coupon is redeemed by the customer; (ii) a coupon expires; or (iii) the likelihood of the points being converted into a coupon and the coupon being redeemed by a customer is remote (“breakage”).

The recorded liability related to these customer loyalty programs totaled \$4 million as of December 31, 2016. The Company estimates the value of the future redemption obligations using statistical formulas that project timing of future point redemptions based on historical levels, including an estimate of the breakage for points that members will never redeem, and an estimate of the points that members will eventually redeem. A ten percent reduction in the estimate of breakage would have increased the estimated liability as of December 31, 2016 by \$1 million.

Direct Marketing Costs. We charge direct marketing costs to expense ratably in relation to revenues over the year in which incurred and, in the case of advertising production costs, in the year the advertisement is first shown. Deferred direct marketing costs, which are classified as prepaid expenses, consist of media and related advertising production costs which will generally be used for the first time in the next fiscal year and have historically not been significant. Our direct marketing expenses were \$332 million, \$327 million and \$328 million in 2016, 2015 and 2014, respectively. We report direct marketing costs in Occupancy and other operating expenses.

Our franchise agreements require our franchisees to fund advertising and marketing expenditures, typically in an amount that is a percentage of sales. Local marketing expenditures are managed by each operator. The Company, as an agent, collects and disburses non-local funds on behalf of the entire system. We record cash received and accounts payable from the administration of such non-local funds in our Consolidated and Combined Balance Sheets. Any unused non-local funds are returned to the system.

Research and Development Expenses. Research and development expenses, which are expensed as incurred, are reported in G&A expenses. Research and development expenses were \$5 million in each of 2016, 2015 and 2014.

Share-Based Compensation. Prior to the separation, all employee equity awards were granted by YUM. Upon the separation, holders of outstanding YUM equity awards generally received both adjusted YUM awards and Yum China awards, or adjusted awards of either YUM or Yum China in their entirety, to maintain the pre-separation intrinsic value of the awards. The modified equity awards have the same terms and conditions as the awards held immediately before the separation, except the number of shares and the price were adjusted. The incremental compensation cost, measured as the excess of the fair value of the award immediately after the modification over the fair value of the award immediately before the modification, based on Black-Scholes option-pricing model was immaterial, and YUM and the Company continue to recognize the unamortized fair value of the awards over the remaining requisite service period as their respective employees continue to provide services. All awards granted following the separation were granted under the Company's Long Term Incentive Plan (the "2016 Plan"). We recognize all share-based payments to employees and directors, including grants of stock options, restricted stock units ("RSU") and stock appreciation rights ("SARs"), in the Consolidated and Combined Financial Statements as compensation cost over the service period based on their fair value on the date of grant. This compensation cost is recognized over the service period on a straight-line basis for awards that actually vest. We present this compensation cost consistent with the other compensation costs for the employee recipient in G&A expenses. Share-based compensation expense includes an allocation of amounts incurred by YUM for services provided on our behalf prior to the separation. See Note 15 for further discussion of YUM's share-based compensation plans.

Impairment or Disposal of Property, Plant and Equipment. Property, plant and equipment ("PP&E") is tested for impairment whenever events or changes in circumstances indicate that the carrying value of the assets may not be recoverable. The assets are not recoverable if their carrying value is less than the undiscounted cash flows we expect to generate from such assets. If the assets are not deemed to be recoverable, impairment is measured based on the excess of their carrying value over their fair value.

For purposes of impairment testing for our restaurants, we have concluded that an individual restaurant is the lowest level of independent cash flows unless our intent is to rebrand restaurants as a group. We review our long-lived assets of such individual restaurants (primarily PP&E and allocated intangible assets subject to amortization) semi-annually for impairment, or whenever events or changes in circumstances indicate that the carrying amount of a restaurant may not be recoverable. We use two consecutive years of operating losses after a restaurant has been open for three years as our primary indicator of potential impairment for our semi-annual impairment testing of these restaurant assets. We evaluate the recoverability of these restaurant assets by comparing the estimated undiscounted future cash flows, which are based on our entity-specific assumptions, to the carrying value of such assets. Our impairment indicator and recoverability tests do not include a deduction for license fees paid to YUM before the separation on October 31, 2016. However, such license fee paid to YUM is included in the impairment indicator and recoverability tests after the separation, as our relationship with YUM changed from the one between a subsidiary and its parent prior to the separation to the one between a licensee and a third-party licensor after the separation. As a result of including license fees paid to YUM, we performed an additional impairment assessment as of November 1, 2016 and recognized incremental restaurant-level impairment of \$17 million. For restaurant assets that are not deemed to be recoverable, we write down an impaired restaurant to its estimated fair value, which becomes its new cost basis. Fair value is an estimate of the price a franchisee would pay for the restaurant and its related assets and is determined by discounting the estimated future after-tax cash flows of the restaurant, which include a deduction for royalties we would receive under a franchise agreement with terms substantially at market. The after-tax cash flows incorporate reasonable assumptions we believe a franchisee would make such as sales growth and margin improvement. The discount rate used in the fair value calculation is our estimate of the required rate-of-return that a franchisee would expect to receive when purchasing a similar restaurant and the related long-lived assets. The discount rate incorporates rates of returns for historical rebranding market transactions and is commensurate with the risks and uncertainty inherent in the forecasted cash flows.

When we believe it is more likely than not a restaurant or groups of restaurants will be rebranded for a price less than their carrying value, but do not believe the restaurant(s) have met the criteria to be classified as held for sale, we review the restaurants for impairment. We evaluate the recoverability of these restaurant assets by comparing estimated sales proceeds plus holding period cash flows, if any, to the carrying value of the restaurant or group of restaurants. For restaurant assets that are not deemed to be recoverable, we recognize impairment for any excess of carrying value over the fair value of the restaurants, which is based on the expected net sales proceeds. To the extent ongoing agreements to be entered into with the franchisee simultaneous with the rebranding are expected to contain terms, such as royalty rates, not at prevailing market rates, we consider the off-market terms in our impairment evaluation. We recognize any such impairment charges in Rebranding gain. Rebranding gain includes the gains or losses from the sales of our restaurants to new and existing franchisees, including any impairment charges discussed above, and the related initial franchise fees. We recognize gains on restaurant rebrandings when the sale transaction closes, the franchisee has a minimum amount of the purchase price in at-risk equity and we are satisfied that the franchisee can meet its financial obligations.

When we decide to close a restaurant, it is reviewed for impairment and depreciable lives are adjusted based on the expected disposal date. Other costs incurred when closing a restaurant such as costs of disposing of the assets as well as other facility-related expenses from previously closed stores are generally expensed as incurred. Additionally, at the date we cease using a property under an operating lease, we record a liability for the net present value of any remaining lease obligations, net of estimated sublease income, if any. Any costs recorded upon store closure as well as any subsequent adjustments to liabilities for remaining lease obligations as a result of lease termination or changes in estimates of sublease income are recorded in Closures and impairment expenses. In the event we are forced to close a store and receive compensation for such closure, that compensation is recorded in Closures and impairment expenses. To the extent we sell assets associated with a closed store, any gain or loss upon that sale is also recorded in Closures and impairment expenses.

Considerable management judgment is necessary to estimate future cash flows, including cash flows from continuing use, terminal value, sublease income and franchising proceeds. Accordingly, actual results could vary significantly from our estimates.

Impairment of Investments in Unconsolidated Affiliates. We record impairment charges related to an investment in an unconsolidated affiliate whenever events or circumstances indicate that a decrease in the fair value of an investment has occurred which is other than temporary. In addition, we evaluate our investments in unconsolidated affiliates for impairment when they have experienced two consecutive years of operating losses.

Government Subsidies. Government subsidies primarily consist of financial subsidies received from provincial and local governments for operating a business in their jurisdictions and compliance with specific policies promoted by the local governments. There are no defined rules and regulations to govern the criteria necessary for companies to receive such benefits, and the amount of financial subsidy is determined at the discretion of the relevant government authorities. Government subsidies are recognized when it is probable that the Company will comply with the conditions attached to them, and the subsidies are received. If the subsidy is related to an expense item, it is recognized as a reduction to the related expense to match the subsidy to the costs that it is intended to compensate. If the subsidy is related to an asset, it is deferred and recorded in other liabilities and then recognized ratably over the expected useful life of the related asset in the Consolidated and Combined Statements of Income.

Income Taxes. Prior to October 31, 2016, the Company's results have historically been included in the consolidated U.S. federal income tax return and U.S. state income tax filings of YUM. The Company has computed its provision for income taxes on a separate return basis in these Consolidated and Combined Financial Statements. The separate return method applies the accounting guidance for income taxes to the standalone financial statements as if the Company was a separate taxpayer and a standalone enterprise for the periods presented prior to October 31, 2016. The calculation of income taxes for the Company on a separate return basis requires a considerable amount of judgment and use of both estimates and allocations. Subsequent to October 31, 2016, the Company became a separate taxpayer and will prepare its own consolidated U.S. federal income tax return and U.S. state income tax filings.

We record deferred tax assets and liabilities for the future tax consequences attributable to temporary differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases as well as operating loss, capital loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those differences or carryforwards are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. Additionally, in determining the need for recording a valuation allowance against the carrying amount of deferred tax assets, we consider the amount of taxable income and periods over which it must be earned, actual levels of past taxable income and known trends and events or transactions that are expected to affect future levels of taxable income. Where we determine that it is more likely than not that all or a portion of an asset will not be realized, we record a valuation allowance.

We recognize the benefit of positions taken or expected to be taken in our tax returns when it is more likely than not, which is a likelihood of more than fifty percent, that the position would be sustained upon examination by tax authorities. A recognized tax position is then measured at the largest amount of benefit that is greater than fifty percent likely of being realized upon settlement. We evaluate these amounts on a quarterly basis to ensure that they have been appropriately adjusted for audit settlements and other events we believe may impact the outcome. Changes in judgment that result in subsequent recognition, derecognition or a change in measurement of a tax position taken in a prior annual period (including any related interest and penalties) are recognized as a discrete item in the interim period in which the change occurs. We recognize accrued interest and penalties related to unrecognized tax benefits as components of our Income tax provision.

We do not record a U.S. deferred tax liability for the excess of the book basis over the tax basis of our investments in foreign subsidiaries to the extent that the basis difference results from earnings that meet the indefinite reversal criteria. This criteria is met if the foreign subsidiary has invested, or will invest, the undistributed earnings indefinitely. The decision as to the amount of undistributed earnings that we intend to maintain in non-U.S. subsidiaries considers items including, but not limited to, forecasts and budgets of financial needs of cash for working capital, liquidity plans and expected cash requirements in the United States.

In November, 2015 the FASB issued ASU No. 2015-17, Balance Sheet Classification of Deferred Taxes (“ASU 2015-17”), to simplify the presentation of deferred taxes on the balance sheet. ASU 2015-17 requires organizations that present a classified balance sheet to classify all deferred taxes as noncurrent assets or noncurrent liabilities. We have elected to early adopt this guidance as of December 31, 2015.

See Note 17 for a further discussion of our income taxes.

Fair Value Measurements. Fair value is the price we would receive to sell an asset or pay to transfer a liability (exit price) in an orderly transaction between market participants. For those assets and liabilities we record or disclose at fair value, we determine fair value based upon the quoted market price, if available. If a quoted market price is not available for identical assets, we determine fair value based upon the quoted market price of similar assets or the present value of expected future cash flows considering the risks involved, including counterparty performance risk if appropriate, and using discount rates appropriate for the duration. The fair values are assigned a level within the fair value hierarchy, depending on the source of the inputs into the calculation.

Level 1 Inputs based upon quoted prices in active markets for identical assets.

Level 2 Inputs other than quoted prices included within Level 1 that are observable for the asset, either directly or indirectly.

Level 3 Inputs that are unobservable for the asset.

Cash and Cash Equivalents. Cash equivalents represent funds we have temporarily invested (with original maturities not exceeding three months), including short-term, highly liquid debt securities. Cash and overdraft balances that meet the criteria for right to offset are presented net on our Consolidated and Combined Balance Sheets.

Short-term Investments. Short-term investments represent time deposits with original maturities of over three months but less than one year when purchased.

Receivables. Trade receivables consisting of royalties from franchisees are generally due within 30 days of the period in which the corresponding sales occur and are classified as Accounts receivable on our Consolidated and Combined Balance Sheets. Our provision for uncollectible franchise receivable balances is based upon pre-defined aging criteria or upon the occurrence of other events that indicate that we may not collect the balance due. Additionally, we monitor the financial condition of our franchisees and record provisions for estimated losses on receivables when we believe it probable that our franchisees will be unable to make their required payments. While we use the best information available in making our determination, the ultimate recovery of recorded receivables is also dependent upon future economic events and other conditions that may be beyond our control. Trade receivables that are ultimately deemed to be uncollectible, and for which collection efforts have been exhausted, are written off against the allowance for doubtful accounts. Receivables due from unconsolidated affiliates were \$53 million and \$19 million as of December 31, 2016 and 2015, respectively.

Receivables from Payment Processors or Aggregators. Receivables from payment processors such as WeChat and Alipay or aggregators are cash due from them for clearing transactions and are included in Prepaid expenses and other current assets. The cash was paid by customers through these payment processors or aggregators for food provided by the Company. The Company considers and monitors the credit worthiness of the third-party payment processors and aggregators used. An allowance for doubtful accounts is recorded in the period in which a loss is determined to be probable. Receivable balances are written off after all collection efforts have been exhausted. As of December 31, 2016, no allowance for doubtful accounts was provided for such receivables.

Inventories. We value our inventories at the lower of cost (computed on the first-in, first-out method) or market.

Property, Plant and Equipment. We state PP&E at cost less accumulated depreciation and amortization. We calculate depreciation and amortization on a straight-line basis over the estimated useful lives of the assets as follows: 20 years for buildings, the lesser of 8 years and remaining lease term for leasehold improvements, 5 to 10 years for restaurant machinery and equipment and 3 to 5 years for capitalized software costs. We suspend depreciation and amortization on assets related to restaurants that are held for sale.

Leases and Leasehold Improvements. The Company leases land, buildings or both for its restaurants. The length of our lease terms, which generally do not have renewal options, is an important factor in determining the appropriate accounting for leases including the initial classification of the lease as capital or operating and the timing of recognition of rent expense over the duration of the lease. We include renewal option periods in determining the term of our leases when failure to renew the lease would impose a penalty on the Company in such an amount that a renewal appears to be reasonably assured at the inception of the lease. The primary penalty to which we are subject is the economic detriment associated with the existence of leasehold improvements which might be impaired if we choose not to continue the use of the leased property. Leasehold improvements are amortized over the shorter of their estimated useful lives or the lease term. We generally do not receive leasehold improvement incentives upon opening a store that is subject to a lease.

We expense rent associated with leased land or buildings while a restaurant is being constructed whether rent is paid or we are subject to a rent holiday. Additionally, certain of the Company's operating leases contain predetermined fixed escalations of the minimum rent during the lease term. For leases with fixed escalating payments and/or rent holidays, we record rent expense on a straight-line basis over the lease term, including any option periods considered in the determination of that lease term. Contingent rentals are generally based on sales levels in excess of stipulated amounts, and thus are not considered minimum lease payments and are included in rent expense when attainment of the contingency is considered probable (e.g., when Company sales occur).

From time to time, we purchase the rights to use government-owned land for a fixed period of time. These land use rights are recorded in Other Assets in our Consolidated and Combined Balance Sheets as we are purchasing the right and are a legal party to the underlying land grant, and are amortized to rent expense on a straight-line basis over the term of the land use right.

Internal Development Costs and Abandoned Site Costs. We capitalize direct costs associated with the site acquisition and construction of a Company unit on that site, including direct internal payroll and payroll-related costs. Only those site-specific costs incurred subsequent to the time that the site acquisition is considered probable are capitalized. If we subsequently make a determination that it is probable a site for which internal development costs have been capitalized will not be acquired or developed, any previously capitalized internal development costs are expensed and included in G&A expenses.

Goodwill and Intangible Assets. From time to time, the Company acquires restaurants from our existing franchisees or acquires another business. Goodwill from these acquisitions represents the excess of the cost of a business acquired over the net of the amounts assigned to assets acquired, including identifiable intangible assets and liabilities assumed. Goodwill is not amortized and has been assigned to reporting units for purposes of impairment testing. Our reporting units are our individual operating segments.

We evaluate goodwill for impairment on an annual basis or more often if an event occurs or circumstances change that indicate impairment might exist. We have selected the beginning of our fourth quarter as the date on which to perform our ongoing annual impairment test for goodwill. We may elect to perform a qualitative assessment for our reporting units to determine whether it is more likely than not that the fair value of the reporting unit is greater than its carrying value. If a qualitative assessment is not performed, or if as a result of a qualitative assessment it is not more likely than not that the fair value of a reporting unit exceeds its carrying value, then the reporting unit's fair value is compared to its carrying value. Fair value is the price a willing buyer would pay for a reporting unit, and is generally estimated using discounted expected future after-tax cash flows from Company-owned restaurant operations and franchise royalties. The discount rate is our estimate of the required rate of return that a third-party buyer would expect to receive when purchasing a business from us that constitutes a reporting unit. We believe the discount rate is commensurate with the risks and uncertainty inherent in the forecasted cash flows. If the carrying value of a reporting unit exceeds its fair value, goodwill is written down to its implied fair value.

If we record goodwill upon acquisition of a restaurant(s) from a franchisee and such restaurant(s) is then sold within two years of acquisition, the goodwill associated with the acquired restaurant(s) is written off in its entirety. If the restaurant is refranchised two years or more subsequent to its acquisition, we include goodwill in the carrying amount of the restaurants disposed of based on the relative fair values of the portion of the reporting unit disposed of in the refranchising and the portion of the reporting unit that will be retained. The fair value of the portion of the reporting unit disposed of in a refranchising is determined by reference to the discounted value of the future cash flows expected to be generated by the restaurant and retained by the franchisee, which includes a deduction for the anticipated, future royalties the franchisee will pay us associated with the franchise agreement entered into simultaneously with the refranchising transition. The fair value of the reporting unit retained is based on the price a willing buyer would pay for the reporting unit and includes the value of franchise agreements. Appropriate adjustments are made if a franchise agreement includes terms that are determined to not be at prevailing market rates. As such, the fair value of the reporting unit retained can include expected cash flows from future royalties from those restaurants currently being refranchised, future royalties from existing franchise businesses and company restaurant operations. As a result, the percentage of a reporting unit's goodwill that will be written off in a refranchising transaction will be less than the percentage of the reporting unit's Company-owned restaurants that are refranchised in that transaction.

We evaluate the remaining useful life of an intangible asset that is not being amortized each reporting period to determine whether events and circumstances continue to support an indefinite useful life. If an intangible asset that is not being amortized is subsequently determined to have a finite useful life, we amortize the intangible asset prospectively over its estimated remaining useful life. Intangible assets that are deemed to have a definite life are generally amortized on a straight-line basis to their residual value.

We evaluate our indefinite-lived intangible assets for impairment on an annual basis or more often if an event occurs or circumstances change that indicate impairments might exist. We perform our annual test for impairment of our indefinite-lived intangible assets at the beginning of our fourth quarter. We may elect to perform a qualitative assessment to determine whether it is more likely than not that the fair value of an indefinite-lived intangible asset is greater than its carrying value. If a qualitative assessment is not performed, or if as a result of a qualitative assessment it is not more likely than not that the fair value of an indefinite-lived intangible asset exceeds its carrying value, then the asset's fair value is compared to its carrying value. Fair value is an estimate of the price a willing buyer would pay for the intangible asset and is generally estimated by discounting the expected future after-tax cash flows associated with the intangible asset.

Our definite-lived intangible assets that are not allocated to an individual restaurant are evaluated for impairment whenever events or changes in circumstances indicate that the carrying amount of the intangible asset may not be recoverable. An intangible asset that is deemed not recoverable on an undiscounted basis is written down to its estimated fair value, which is our estimate of the price a willing buyer would pay for the intangible asset based on discounted expected future after-tax cash flows. For purposes of our impairment analysis, we update the cash flows that were initially used to value the definite-lived intangible asset to reflect our current estimates and assumptions over the asset's future remaining life.

Financial Instruments. We account for derivative instruments and liability-classified equity contracts (e.g., warrants) as either assets or liabilities in the Consolidated and Combined Balance Sheets. The financial instruments are recorded at their respective fair value as determined on the day of issuance and subsequently adjusted to the fair value at each reporting date. Changes in the fair value of financial instruments are recognized periodically in the Consolidated and Combined Statements of Income (Loss). The estimated fair values of derivative instruments and liability-classified equity contracts are determined at discrete points in time using standard valuation techniques. See Note 13 for further discussion.

Guarantees. We account for guarantees in accordance with ASC Topic 460 ("ASC 460"), *Guarantees*. Accordingly, the Company evaluates its guarantees to determine whether (a) the guarantee is specifically excluded from the scope of ASC 460, (b) the guarantee is subject to ASC 460 disclosure requirements only, but not subject to the initial recognition and measurement provisions, or (c) the guarantee is required to be recorded in the financial statements at fair value. The Company provides: (i) indemnifications to certain investors and other parties for certain losses suffered or incurred by the indemnified party in connection with third-party claims; and (ii) indemnifications of officers and directors against third-party claims arising from the services they provide to the Company. To date, the Company has not incurred costs as a result of these obligations and does not expect to incur material costs in the future. Accordingly, the Company has not accrued any liabilities in the Consolidated and Combined Balance Sheets related to these indemnifications.

Asset Retirement Obligations. We recognize an asset and a liability for the fair value of a required asset retirement obligation ("ARO") when such an obligation is incurred. The Company's AROs are primarily associated with leasehold improvements which, at the end of the lease, the Company is contractually obligated to remove in order to comply with the lease agreement. As such, we amortize the asset on a straight-line basis over the lease term and accrete the liability to its nominal value using the effective interest method over the lease term.

Contingencies. The Company records accruals for certain of its outstanding legal proceedings or claims when it is probable that a liability will be incurred and the amount of loss can be reasonably estimated. The Company evaluates, on a quarterly basis, developments in legal proceedings or claims that could affect the amount of any accrual, as well as any developments that would make a loss contingency both probable and reasonably estimable. The Company discloses the amount of the accrual if it is material.

Retirement Plans. Certain of the Company's employees participate in noncontributory defined benefit plans and post-retirement medical plans sponsored by YUM prior to October 31, 2016. For these plans, the Company considers them to be part of multi-employer plans. YUM has allocated expenses related to our employees' participation in these plans in our Consolidated and Combined Statements of Income. However, our Combined Balance Sheets do not reflect any assets or liabilities related to these plans. We consider the expense allocation methodology and results to be reasonable for the periods prior to October 31, 2016. See Note 3 for additional information. Subsequent to the separation, employees participating in YUM's plans were enrolled in the Yum China Holdings, Inc. Leadership Retirement Plan ("YCHLRP"), as discussed below.

For executives who were hired or re-hired after September 30, 2001, YUM has implemented the Leadership Retirement Plan (“YUM LRP”). This is an unfunded, unsecured account-based retirement plan which allocates a percentage of pay to an account payable to the executive following the executive’s separation of employment from YUM or attainment of age 55. The Company adopted YCHLRP upon the separation, and the terms of the YCHLRP are substantially similar to the terms of the YUM LRP. The Company also offers other defined contribution plans to employees. The total contribution for such employee benefits was expensed as incurred. The Company has no additional legal obligation or liabilities for the benefits beyond the paid and accrued amounts. See Note 14 for additional information.

PRC Value-Added Tax. On January 1, 2012, the Chinese State Council officially launched a retail tax structure reform program (“VAT pilot program” or “VAT reform”), applicable to businesses in selected industries, whereby entities in these industries would pay VAT instead of business tax (“BT”). Since January 1, 2012, the Chinese government has gradually expanded the scope of the VAT reform to cover most service sectors. Effective as of May 1, 2016, the Chinese government extended the VAT reform to all remaining sectors still subject to BT, including the catering sector. Thus, the Company has been subject to VAT within the normal course of its restaurant business nationwide since May 1, 2016.

Entities that are VAT general taxpayers are permitted to offset qualified input VAT paid to suppliers against their output VAT upon receipt of appropriate supplier VAT invoices on an entity by entity basis. When the output VAT exceeds the input VAT, the difference is remitted to tax authorities, usually on a monthly basis; whereas when the input VAT exceeds the output VAT, the difference is treated as an input VAT credit asset which can be carried forward indefinitely to offset future net VAT payables. VAT related to purchases and sales which have not been settled at the balance sheet date is disclosed separately as an asset and liability, respectively, in the Consolidated and Combined Balance Sheets. At each balance sheet date, the Company reviews the outstanding balance of any net VAT credit asset for recoverability assessment. We evaluate the recoverability of the net VAT credit asset based on our estimated operating results and capital spending, which inherently includes significant assumptions subject to change.

As of December 31, 2016, an input VAT credit asset of \$80 million and payable of \$3 million were recorded in Other assets and Accounts payable and other current liabilities, respectively, in the Consolidated and Combined Balance Sheets. The Company has not made an allowance for the recoverability of the input VAT credit asset, as the balance is expected to be utilized to offset against net VAT payables more than one year from December 31, 2016. Any input VAT credit asset would be classified as Prepaid expenses and other current assets if the Company expected to use the credit within one year.

Earnings Per Share. Basic earnings per share represent net earnings to common stockholders divided by the weighted-average number of common shares outstanding for the period. Diluted earnings per share reflect the potential dilution that could occur if securities or other contracts to issue common shares were exercised or converted into common shares. See Note 4 for further information.

Parent Company Investment. Parent Company Investment in the Consolidated and Combined Balance Sheets represents YUM’s historical investment in the Company, the Company’s accumulated net earnings after taxes, and the net effect of transactions with and allocations from YUM. The Consolidated and Combined Statements of Equity include net cash transfers to and from YUM and the Company. All intercompany transactions that are not cash settled through Parent Company Investment in the accompanying Consolidated and Combined Balance Sheets are considered to be settled at the time the transaction is recorded. The total net effect of the settlement of these transactions is reflected in financing activities in the accompanying Consolidated and Combined Statements of Cash Flows. Upon the separation, Parent Company Investment was adjusted as a result of settlement of certain assets and liabilities with YUM and formed the Company’s common stock and additional paid-in capital.

Note 3 – Transactions with Parent

Prior to the separation, there existed a parent-subsiary relationship between YUM and the Company. We had the following transactions with YUM for the ten months ended October 31, 2016 and the years ended December 31, 2015 and 2014:

Allocation of Corporate Expenses

YUM historically performed centralized corporate functions on our behalf prior to October 31, 2016. Accordingly, certain YUM costs have been allocated to the Company and reflected as expenses in the Combined Financial Statements. Management considers the allocation methodologies used to be reasonable and appropriate reflections of the historical expenses attributable to the Company. The expenses reflected in the Combined Financial Statements may not be indicative of the actual expenses that would have been incurred during the periods presented if we had operated as a separate, standalone entity.

Corporate expense allocations primarily relate to centralized corporate functions, including finance, accounting, treasury, tax, legal, internal audit and risk management functions. In addition, corporate expense allocations include, among other costs, IT maintenance, professional fees for legal services and expenses related to litigation, investigations, or similar matters. Corporate allocations of \$11 million, \$12 million and \$11 million were allocated to the Company during the ten months ended October 31, 2016 and the years ended December 31, 2015 and 2014, respectively, and have been included in G&A expenses in the Consolidated and Combined Statements of Income. All of the corporate allocations of costs are deemed to have been incurred and settled through Parent Company Investment in the Consolidated and Combined Balance Sheets in the period where the costs were recorded. Following the separation from YUM, we perform these functions using our own resources or purchased services.

License Fee

The Consolidated and Combined Statements of Income include a fee that was historically paid to YUM comprised of initial fees and continuing fees equal to 3% of our Company and franchise sales prior to October 31, 2016. Total license fees paid to YUM during the ten months ended October 31, 2016 and the years ended December 31, 2015 and 2014 are reflected in the table below:

	10 months ended	Year ended	
	October 31, 2016	December 31, 2015	December 31, 2014
Initial fees – Company	\$ 9	\$ 18	\$ 17
Initial fees – Franchise	2	3	2
Continuing fees – Company	163	201	200
Continuing fees – Franchise	42	47	46
Total	<u>\$ 216</u>	<u>\$ 269</u>	<u>\$ 265</u>

Cash Management and Treasury

The Company funds its operations through cash generated from the operation of its Company-owned stores, franchise operations and dividend payments from unconsolidated affiliates. Prior to October 31, 2016, excess cash has historically been repatriated to YUM through intercompany loans or dividends. Transfers of cash both to and from YUM are included within Parent Company Investment in the Consolidated and Combined Balance Sheets. YUM has issued debt for general corporate purposes but in no case has any such debt been guaranteed or assumed by the Company or otherwise secured by the assets of the Company. As YUM's debt and related interest is not directly attributable to the Company, no such amounts have been allocated to the Consolidated and Combined Financial Statements.

Note 4 – Earnings Per Common Share (“EPS”)

On October 31, 2016, YUM's shareholders of record as of October 19, 2016 received one share of Yum China common stock for every one share of YUM's common stock held as of the record date. For periods ended October 31, 2016 and prior, basic and diluted earnings per share were computed using the number of shares of Yum China common stock outstanding as of October 31, 2016, the date on which the Yum China common stock was distributed to YUM's shareholders. The same number of shares was used to calculate basic and diluted earnings per share for years 2015 and 2014 since there were no dilutive securities until after the separation.

The following table summarizes the components of basic and diluted earnings per share:

	2016	2015	2014
Net Income (Loss) – Yum China Holdings, Inc.	\$ 502	\$ 323	\$ (7)
Weighted-average common shares outstanding (for basic calculation) ^(a)	367,744,992	363,758,219	363,758,219
Effect of dilutive share-based employee compensation ^(a)	1,398,846	—	—
Weighted-average common and dilutive potential common shares outstanding (for diluted calculation)	369,143,838	363,758,219	363,758,219
Basic Earnings (Loss) Per Share	\$ 1.36	\$ 0.89	\$ (0.02)
Diluted Earnings (Loss) Per Share	\$ 1.36	\$ 0.89	\$ (0.02)
Employee stock options, stock appreciation rights and warrants excluded from the diluted EPS computation ^(b)	16,987,578	—	—

(a) As a result of the separation, shares of Yum China common stock were distributed to YUM's shareholders of record as of October 19, 2016 and included in the calculated weighted-average common shares outstanding. Holders of outstanding YUM equity awards generally received both adjusted YUM awards and Yum China awards, or adjusted awards of either YUM or Yum China in their entirety, to maintain the pre-separation intrinsic value of the awards. Any subsequent exercise of these awards, whether held by the Company's employees or YUM's employees, would increase the number of common shares outstanding. The outstanding equity awards are included in the computation of diluted EPS, if there is dilutive effect. See Note 15 for a further discussion of share-based compensation.

(b) These unexercised employee stock options, stock appreciation rights, and warrants were not included in the computation of diluted EPS because to do so would have been antidilutive for the years presented.

Note 5 – Items Affecting Comparability of Net Income and Cash Flows

Little Sheep Impairment

On February 1, 2012, we acquired an additional 66% interest in Little Sheep Group Limited (“Little Sheep”) for \$540 million, net of cash acquired of \$44 million, increasing our ownership to 93%. The primary assets recorded as a result of the acquisition and resulting consolidation of Little Sheep were the Little Sheep trademark and goodwill of approximately \$400 million and \$375 million, respectively.

Sustained declines in sales and profits in 2013 resulted in a determination that the Little Sheep trademark, goodwill and certain restaurant level PP&E were impaired. As a result, we recorded impairment charges to the trademark, goodwill and PP&E of \$69 million, \$222 million and \$4 million, respectively, during the year ended December 31, 2013. We also recorded tax benefit of \$18 million and loss of \$19 million attributable to noncontrolling interest in connection with the impairment charges recorded. The Little Sheep business continued to underperform during 2014 and a significant number of Company-operated restaurants were closed or refranchised during 2014 with future plans calling for further focus on franchise-ownership for the Concept. As a result, we recorded impairment charges to the trademark, goodwill, and PP&E of \$284 million, \$160 million and \$14 million, respectively, and a \$5 million impairment of our equity method investment in a meat processing business that supplies lamb to Little Sheep during the year ended December 31, 2014. We also recorded tax benefit of \$76 million and loss of \$26 million attributable to noncontrolling interest in connection with the impairment charges recorded.

The losses related to Little Sheep that have occurred concurrent with our trademark and goodwill impairments in 2014 and 2013 were included in Closures and impairment expenses, net in our Consolidated and Combined Statement of Income, but were not allocated to any segment for performance reporting purposes. There were no impairment charges related to Little Sheep during the years ended December 31, 2016 and 2015. During the year ended December 31, 2016, we recorded a tax benefit of \$26 million related to the legal entity restructuring of our Little Sheep business.

Refranchising Gain, net

The Refranchising gain, net by reportable segment and All Other Segments is presented below. We do not allocate such gains and losses to our segments for performance reporting purposes.

	Refranchising gain, net		
	2016	2015	2014
KFC	\$ 14	\$ 8	\$ 17
Pizza Hut Casual Dining	1	3	—
All Other Segments	—	2	—
Total Company	<u>\$ 15</u>	<u>\$ 13</u>	<u>\$ 17</u>

Store Closure and Impairment Activity

Store closure income (costs) and Store impairment charges by reportable segment and All Other Segments are presented below. These tables exclude \$463 million of Little Sheep impairment losses in 2014 and \$17 million of incremental restaurant-level impairment upon the separation in 2016, which were not allocated to any segment for performance reporting purposes.

	2016			
	Total Company	KFC	Pizza Hut Casual Dining	All Other Segments
Store closure income (costs) ^(a)	\$ 9	\$ 7	\$ 1	\$ 1
Store impairment charges	(70)	(48)	(18)	(4)
Closure and impairment expenses	<u>\$ (61)</u>	<u>\$ (41)</u>	<u>\$ (17)</u>	<u>\$ (3)</u>

	2015			
	Total Company	KFC	Pizza Hut Casual Dining	All Other Segments
Store closure income (costs) ^(a)	\$ 6	\$ 7	\$ 2	\$ (3)
Store impairment charges	(70)	(57)	(10)	(3)
Closure and impairment expenses	<u>\$ (64)</u>	<u>\$ (50)</u>	<u>\$ (8)</u>	<u>\$ (6)</u>

	2014			
	Total Company	KFC	Pizza Hut Casual Dining	All Other Segments
Store closure income (costs) ^(a)	\$ —	\$ 2	\$ 1	\$ (3)
Store impairment charges	(54)	(43)	(3)	(8)
Closure and impairment expenses	<u>\$ (54)</u>	<u>\$ (41)</u>	<u>\$ (2)</u>	<u>\$ (11)</u>

(a) Store closure income (costs) include lease reserves established when we cease using a property under an operating lease and subsequent adjustments to those reserves, other facility-related expenses from previously closed stores and proceeds from forced store closures. Remaining lease obligations for the closed stores were not material at December 31, 2016 or December 31, 2015.

Redeemable Noncontrolling Interest

At December 31, 2015, the redeemable noncontrolling interest comprised the 7% ownership interest in Little Sheep held by the Little Sheep founding shareholders, and was classified outside of permanent equity on our Consolidated and Combined Balance Sheets due to redemption rights held by the founding Little Sheep shareholders. During the year ended December 31, 2016, the Little Sheep founding shareholders sold their remaining 7% Little Sheep ownership interest to the Company pursuant to their redemption rights. The difference between the purchase price of less than \$1 million, which was determined using a non-fair value based formula pursuant to the agreement governing the redemption rights, and the carrying value of their redeemable noncontrolling interest was recorded as an \$8 million loss attributable to noncontrolling interests during the year ended December 31, 2016. See Note 8 for additional information.

Losses Associated with Sale of Aircraft

During 2015, we made the decision to dispose of a corporate aircraft in China and recognized a loss of \$15 million associated with the sale of the aircraft for the year ended December 31, 2015. We completed the sale during 2016. The sale proceeds of \$19 million was greater than the net book value of \$17 million of the aircraft at the time of disposal, which resulted in a reversal of \$2 million of the previously recognized loss.

Incremental Restaurant-Level Impairment upon Separation

Incremental restaurant-level impairment represents additional impairment as a result of including the impact from the license fee paid to YUM on the individual restaurants future cash flow, which is equal to 3% of net system sales. Such license fee did not impact the impairment assessment prior to the separation as it was considered an intercompany charge at the time, whereas it became a charge from a third party after the separation and has been considered in the impairment assessment. See Note 13 for additional information.

Investment Agreements with Strategic Investors

In connection with the investment agreement with strategic investors entered into on September 1, 2016, Yum China issued 19,145,169.42 shares of common stock on November 1, 2016, subject to Post-Closing Adjustments by December 30, 2016, and warrants to purchase additional shares of common stock. The Post-Closing Adjustment and the warrants were accounted for as derivative instruments and liability-classified equity contracts, respectively. These financial instruments were initially measured at fair value on the date of issuance, with subsequent changes in fair value of \$21 million included in earnings during the year ended December 31, 2016. No subsequent fair value measurements were recognized after December 30, 2016. See Note 11 for additional information.

Note 6 – Franchise Fees and Income

	2016	2015	2014
Initial fees, including renewal fees	\$ 10	\$ 9	\$ 7
Initial franchise fees included in Refranchising gain, net	(4)	(3)	(3)
	6	6	4
Continuing fees and rental income	124	114	109
Franchise fees and income	<u>\$ 130</u>	<u>\$ 120</u>	<u>\$ 113</u>

Note 7 – Other Income, net

	2016	2015	2014
Equity income from investments in unconsolidated affiliates	\$ 54	\$ 41	\$ 30
China poultry supply insurance recovery ^(a)	3	5	25
Reversal of (provision for) losses associated with sale of aircraft	2	(15)	—
Foreign exchange net loss and other	(3)	(5)	(4)
Other income, net	<u>\$ 56</u>	<u>\$ 26</u>	<u>\$ 51</u>

(a) Recoveries related to lost profits associated with a 2012 poultry supply incident.

Note 8 – Supplemental Balance Sheet Information

<u>Accounts Receivables, net</u>	2016	2015
Accounts receivables, gross	\$ 76	\$ 35
Allowance for doubtful accounts	(2)	(2)
Accounts receivables, net	<u>\$ 74</u>	<u>\$ 33</u>

<u>Prepaid Expenses and Other Current Assets</u>	2016	2015
Assets held for sale ^(a)	\$ —	\$ 18
Prepaid rent	39	53
Other prepaid expenses and current assets ^(b)	81	81
Prepaid expenses and other current assets	<u>\$ 120</u>	<u>\$ 152</u>

(a) Reflects the carrying value of a corporate aircraft in China (See Note 5).

(b) Includes receivables of \$16 million and insignificant amounts due from payment processors or aggregators as of December 31, 2016 and 2015, respectively (See Note 2).

<u>Property, Plant and Equipment</u>	2016	2015
Buildings and improvements	\$ 2,029	\$ 2,231
Capital leases, primarily buildings	29	35
Machinery and equipment	1,081	1,171
Property, plant and equipment, gross	3,139	3,437
Accumulated depreciation and amortization	(1,492)	(1,596)
Property, plant and equipment, net	<u>\$ 1,647</u>	<u>\$ 1,841</u>

Depreciation and amortization expense related to property, plant and equipment was \$385 million, \$408 million and \$392 million in 2016, 2015 and 2014, respectively.

<u>Accounts Payable and Other Current Liabilities</u>	2016	2015
Accounts payable	\$ 480	\$ 438
Accrued capital expenditures	132	153
Accrued compensation and benefits	191	180
Accrued taxes, other than income taxes	14	42
Other current liabilities	154	113
Accounts payable and other current liabilities	<u>\$ 971</u>	<u>\$ 926</u>

<u>Other Liabilities and Deferred Credits</u>	2016	2015
Deferred escalating minimum rent	\$ 153	\$ 162
Other noncurrent liabilities and deferred credits	99	72
Other liabilities and deferred credits	<u>\$ 252</u>	<u>\$ 234</u>

Noncontrolling Interests

Noncontrolling interests represent the ownership interests of minority shareholders of the entities that operate KFC restaurants in Beijing and Shanghai, China. At December 31, 2015, the redeemable noncontrolling interest comprised the 7% ownership interest in Little Sheep held by the Little Sheep founding shareholders, and was classified outside of permanent equity on our Consolidated and Combined Balance Sheets due to redemption rights held by the founding Little Sheep shareholders. During the year ended December 31, 2016, the Little Sheep founding shareholders sold their remaining 7% Little Sheep ownership interest to the Company pursuant to their redemption rights. The difference between the purchase price of less than \$1 million, which was determined using a non-fair value based formula pursuant to the agreement governing the redemption rights, and the carrying value of their redeemable noncontrolling interest was recorded as an \$8 million loss attributable to noncontrolling interests during the year ended December 31, 2016. Consistent with our 2012 gain on the acquisition of Little Sheep and subsequent impairments of Little Sheep goodwill and intangibles in 2013 and 2014, the loss attributable to noncontrolling interests is not being allocated to any segment operating results. A reconciliation of the beginning and ending carrying amount of the equity attributable to noncontrolling interests is as follows:

	Noncontrolling Interests	Redeemable Noncontrolling Interest
Balance at December 31, 2014	\$ 57	\$ 9
Net income (loss) – noncontrolling interests	6	(1)
Acquisition of noncontrolling interests	(1)	—
Currency translation adjustments	(4)	(2)
Balance at December 31, 2015	\$ 58	\$ 6
Net income – noncontrolling interests	19	1
Noncontrolling interest loss upon redemption	—	(8)
Dividends declared	(7)	—
Currency translation adjustments	(4)	1
Balance at December 31, 2016	<u>\$ 66</u>	<u>\$ —</u>

Note 9 – Goodwill and Intangible Assets

The changes in the carrying amount of goodwill are as follows:

	Total Company	KFC	Pizza Hut Casual Dining	All Other Segments ^(a)
Balance as of December 31, 2014				
Goodwill, gross	\$ 471	\$ 78	\$ 11	\$ 382
Accumulated impairment losses	(382)	—	—	(382)
Disposals and other, net ^(b)	(4)	(3)	(1)	—
Balance as of December 31, 2015				
Goodwill, gross	467	75	10	382
Accumulated impairment losses	(382)	—	—	(382)
Disposals and other, net ^(b)	(6)	(5)	(1)	—
Balance as of December 31, 2016				
Goodwill, gross	461	70	9	382
Accumulated impairment losses	(382)	—	—	(382)
Goodwill, net	<u>\$ 79</u>	<u>\$ 70</u>	<u>\$ 9</u>	<u>\$ —</u>

- (a) Goodwill, gross and Accumulated impairment losses represent Little Sheep goodwill and related impairment.
- (b) Disposals and other, net includes the impact of foreign currency translation on existing balances and goodwill write-offs associated with refranchising.

Intangible assets, net as of December 31, 2016 and 2015 are as follows:

	2016		2015			
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Definite-lived intangible assets						
Reacquired franchise rights	\$ 93	\$ (71)	\$ 22	\$ 100	\$ (66)	\$ 34
Other	26	(13)	13	30	(13)	17
	<u>\$ 119</u>	<u>\$ (84)</u>	<u>\$ 35</u>	<u>\$ 130</u>	<u>\$ (79)</u>	<u>\$ 51</u>
Indefinite-lived intangible assets						
Little Sheep trademark	\$ 53	—	\$ 53	\$ 56	—	\$ 56
Total intangible assets	<u>\$ 172</u>	<u>\$ (84)</u>	<u>\$ 88</u>	<u>\$ 186</u>	<u>\$ (79)</u>	<u>\$ 107</u>

Amortization expense for definite-lived intangible assets was \$12 million in 2016, \$13 million in 2015 and \$14 million in 2014. Amortization expense for definite-lived intangible assets will approximate \$12 million in 2017, \$12 million in 2018, \$4 million in 2019, \$2 million in 2020 and \$1 million in 2021.

Note 10 – Credit Facilities

As of December 31, 2016, the Company had credit facilities of RMB2,300 million (approximately \$330 million) in the aggregate. During 2016, the Company entered into six new revolving credit facilities of RMB700 million, RMB300 million, RMB200 million, RMB300 million, RMB300 million and RMB200 million (approximately \$287 million in the aggregate).

As of December 31, 2015, the Company had an external bank credit agreement for each of two RMB300 million revolving credit facilities (approximately \$92 million in aggregate). The three-year credit facility matured on April 30, 2016 and was not renewed. The one-year credit facility was renewed on February 17, 2016.

The credit facilities have terms ranging from 1 to 3 years. Each credit facility bears interest based on the prevailing rate stipulated by the People's Bank of China and contains financial covenants including, among other things, limitations on certain additional indebtedness and liens, and certain other transactions specified in the respective agreement. Each credit facility contains cross-default provision whereby our failure to make any payment on a principal amount from any credit facility will constitute a default on the respective agreement. Interest on any outstanding borrowings is due at least monthly. As of December 31, 2016, the full amount of borrowings were available to us under each credit facility.

Note 11 – Investment Agreements with Strategic Investors

On September 1, 2016, YUM and the Company entered into investment agreements (the “Investment Agreements”) with each of Pollos Investment L.P., an affiliate of Primavera Capital Group (“Primavera”), and API (Hong Kong) Investment Limited, an affiliate of Zhejiang Ant Small and Micro Financial Services Group Co., Ltd. (“Ant Financial” and, together with Primavera, the “Investors”). Pursuant to the Investment Agreements, on November 1, 2016 (“Closing Date”), Primavera and Ant Financial invested \$410 million and \$50 million, respectively, for a collective \$460 million investment (the “Investment”) in the Company in exchange for: (i) shares of Yum China common stock representing in the aggregate 5% of Yum China common stock issued and outstanding immediately following the separation subject to Post-Closing Adjustment for a final aggregate ownership of between 4.3% and 5.9% in Yum China and (ii) two tranches of warrants (the “Warrants”), which will be issued to the Investors approximately 70 days after the separation, exercisable by the Investors for an approximate additional 4% ownership, in the aggregate, of Yum China common stock issued and outstanding after the separation, taking into account the shares previously issued to the Investors. Immediately before the closing of the Investment, Yum China had 363,758,219 shares of common stock issued and outstanding, with a par value US\$0.01 per share. Pursuant to the Investment Agreements, on November 1, 2016, Yum China issued 17,064,172.74 and 2,080,996.68 shares of common stock (the “Closing Shares”) at US\$24.03 per share (“Closing Price”) to Primavera and Ant Financial, respectively, subject to adjustment as described below.

Pursuant to the Investment Agreements, the Investors and the Company determined the volume weighted average trading price (“VWAP”) per share of Company common stock over the trading days occurring over the period from December 1, 2016 to December 30, 2016 (the “Measurement Period”), and discounted such VWAP by 8% (the “Adjusted VWAP Price Per Share”).

Since the Adjusted VWAP Price Per Share of \$25.05 exceeded the Closing Price of US\$24.03 paid by the Investors at the Closing Date, on January 9, 2017, the Company repurchased from Primavera and Ant Financial 699,394.74 and 85,291.68 shares of common stock, respectively, at par value of \$0.01 per share, based on the Adjusted VWAP Price Per Share as determined on December 30, 2016. The repurchased shares were included in Treasury Stock as of December 31, 2016 in the Consolidated and Combined Financial Statements.

In addition, pursuant to the terms of the Investment Agreements, on January 9, 2017, Yum China issued to each of the Investors two tranches of Warrants. Upon exercise, the first tranche of Warrants provide Primavera and Ant Financial with the right to purchase 7,309,057 and 891,348 shares of Yum China common stock, respectively, at an exercise price of \$31.40 per share. The second tranche of Warrants provide Primavera and Ant Financial with the right to purchase the same number of shares of Yum China common stock purchasable by Primavera and Ant Financial under the first tranche of Warrants, at an exercise price of \$39.25 per share. The exercise price for the Warrants was based on \$12 billion and \$15 billion for the first tranche and second tranche, respectively, divided by the number of shares of common stock, including the Closing Shares after the Post-Closing Adjustment, issued and outstanding as of the Closing Date. The Warrants may be exercised at any time through October 31, 2021 and contain customary anti-dilution protections.

As a result of the issuance of the Closing Shares and the Post-Closing Adjustment (excluding shares issuable upon exercise of the Warrants), Primavera and Ant Financial collectively beneficially owned approximately 4.8% of the outstanding shares of Yum China common stock as of January 9, 2017, or approximately 8.7% of the outstanding shares of Yum China common stock as of January 9, 2017 assuming the full exercise of both tranches of Warrants by each of the Investors.

The Post-Closing Adjustment was accounted for as a combination of a purchased call and a written put. In accordance with ASC Topic 480 (“ASC 480”), *Distinguishing Liabilities from Equity*, the feature should be accounted for as a liability or an asset, as the monetary value of the obligation varies inversely in relation to changes in the fair value of Yum China common stock and Yum China can net share settle the contract. Therefore, the Post-Closing Adjustment was measured as a derivate asset at a fair value of \$1.3 million on November 1, 2016, with the subsequent increase in fair value of \$19.2 million included in earnings until December 30, 2016. As the Post-Closing Adjustment was effectively settled and included in Treasury Stock on December 30, 2016, no subsequent fair value measurement was required.

The Warrants were recorded as liability-classified equity contracts in accordance with ASC Topic 815 (“ASC 815”), *Derivatives and Hedging*, as the number of Warrants cannot be determined until the Post-Closing Adjustment is made and, therefore, the settlement amount is not fixed. They were measured at fair value of \$97.1 million as of November 1, 2016, with subsequent decrease in fair value of \$2.1 million included in earnings until December 30, 2016, when the Warrants were reclassified to equity at the then fair value of \$95 million. After the Post-Closing Adjustment was resolved, the number of Warrants to be issued became fixed, and the Warrants were considered indexed to the Yum China’s own stock. As share settlement is within Yum China’s control, the Warrants met the equity classification criteria on December 30, 2016 and no subsequent fair value measurement was required.

Total cash proceeds of \$460 million from the closing of the Investment were first allocated to the Post-Closing Adjustment and Warrants based on their fair value on November 1, 2016, with the residual value of \$364 million allocated to the shares of common stock issued.

In connection with and at the closing of the Investment, on November 1, 2016, Yum China and the Investors entered into a shareholders agreement, relating to rights and obligations of the Investors as holders of Yum China common stock and Warrants. Under the terms of the shareholders agreement, Primavera is entitled to designate one member of Yum China’s board of directors and has the right to designate one non-voting board observer to Yum China’s board of directors. In addition, Ant Financial also has the right to designate one non-voting board observer to Yum China’s board of directors. If Primavera no longer meets certain shareholding requirements, then three years after such time, Ant Financial will lose its right to designate a board observer (unless such right has been previously terminated pursuant to the terms of the shareholders agreement).

Note 12 – Leases

At December 31, 2016, we operated more than 6,000 restaurants, leasing the underlying land and/or building, with our commitments expiring within 20 years from the inception of the lease. In addition, the Company subleases approximately 180 properties to franchisees. Most leases require us to pay related executory costs, which include property taxes, maintenance and insurance.

We also lease office space for headquarters and support functions, as well as certain office and restaurant equipment. We do not consider any of these individual leases material to our operations.

Future minimum commitments and amounts to be received as lessor or sublessor under non-cancelable leases are set forth below:

	Commitments		Lease
	Capital	Operating	Receivables Operating
2017	\$ 3	\$ 444	\$ 16
2018	3	413	16
2019	3	383	15
2020	3	354	13
2021	3	314	11
Thereafter	30	1,140	24
	<u>\$ 45</u>	<u>\$ 3,048</u>	<u>\$ 95</u>

At December 31, 2016 and 2015, the present value of minimum payments under capital leases was \$30 million and \$35 million, respectively. The current portion of capital lease obligations was \$1 million and \$1 million in 2016 and 2015, respectively, and is classified in Accounts payable and other current liabilities.

The details of rental expense and income are set forth below:

	2016	2015	2014
Rental expense			
Minimum	\$ 470	\$ 516	\$ 523
Contingent	250	260	265
	<u>\$ 720</u>	<u>\$ 776</u>	<u>\$ 788</u>
Rental income	<u>\$ 26</u>	<u>\$ 24</u>	<u>\$ 20</u>

Note 13 – Fair Value Disclosures

As of December 31, 2016 the carrying values of cash and cash equivalents, short-term investments, accounts receivable and accounts payable approximated their fair values because of the short-term nature of these instruments.

In addition, certain of the Company's assets, such as property, plant and equipment, goodwill and intangible assets, are measured at fair value on a non-recurring basis, if determined to be impaired. The financial instruments are measured at fair value on a non-recurring basis, as they were issued and reclassified into equity within the same year.

The following table presents expense recognized from all non-recurring fair value measurements during the years ended December 31, 2016, 2015 and 2014. All fair value measurements were based on unobservable inputs (Level 3). These amounts exclude fair value measurements made for restaurants that were subsequently closed or refranchised prior to those respective year-end dates.

	2016	2015	2014
Little Sheep impairment ^(a)	\$ —	\$ —	\$ 463
Restaurant-level impairment ^(b)	58	51	35
Incremental restaurant-level impairment upon separation ^(c)	17	—	—
Changes in fair value of financial instruments ^(d)	(21)	—	—
Total	<u>\$ 54</u>	<u>\$ 51</u>	<u>\$ 498</u>

- (a) Except for the Little Sheep trademark, which had a carrying value of \$53 million at December 31, 2016, the remaining carrying value of assets measured at fair value due to the 2014 Little Sheep impairments (Level 3) was insignificant. Our 2014 fair value estimate of the Little Sheep trademark was determined using a relief-from-royalty valuation approach that included future revenues as a significant input and a discount rate of 13% as our estimate of the required rate-of-return that a third party buyer would expect to receive when purchasing the trademark. The primary drivers of the trademark's fair value are franchise revenue growth and revenues associated with a wholly-owned business that sells seasoning to retail customers. Franchise revenue growth reflected annual same store sales growth of 4% and approximately 35 new franchise units per year, partially offset by approximately 25 franchise closures per year. The retail seasoning business was forecasted to generate sales growth consistent with historical results. Our 2016 and 2015 fair value estimates exceeded their carrying values using similar assumptions and methods as those used in 2014.
- (b) Restaurant-level impairment charges are recorded in Closures and impairment expenses, net and resulted primarily from our semi-annual impairment evaluation of long-lived assets of individual restaurants that were being operated at the time of impairment and had not been offered for refranchising. The fair value measurements used in these impairment evaluations were based on discounted cash flow estimates using unobservable inputs (Level 3). The remaining net book value of assets measured at fair value during the years ended December 31, 2016, 2015 and 2014 was insignificant.
- (c) Incremental restaurant-level impairment represents additional impairment as a result of including the impact from the license fee paid to YUM on the individual restaurants future cash flow, which is equal to 3% of net system sales. Such license fee did not impact the impairment assessment prior to the separation as it was considered an intercompany charge at the time, whereas it became a charge from a third party after the separation and therefore should be considered in the impairment assessment. The remaining net book value of assets measured at fair value during the year ended December 31, 2016 was insignificant.

- (d) The Post-Closing Adjustment and the warrants from the investment with strategic investors were accounted for as derivative instruments and liability-classified equity contracts, respectively (see Note 11). These financial instruments were initially measured at fair value as of November 1, 2016, the date when shares of common stock were issued, and subject to subsequent fair value measurement until December 30, 2016. They are classified within Level 3 because their fair values are based on inputs that are unobservable in the market. The Company adopted the Monte-Carlo Simulation model (the “MCS” model) and Black-Scholes option-pricing model (the “BS” model) in deriving the initial fair values of the Post-Closing Adjustment and the warrants, respectively. On December 30, 2016, when the Adjusted VWAP Price Per Share was determined, the Post-Closing Adjustment was remeasured at fair value of \$20.5 million based on 784,686.42 shares of common stock to be repurchased from the Investors at the closing price of \$26.12 per share. The Warrants were remeasured at fair value of \$95 million using the BS option pricing model with assumptions as of December 30, 2016. The key assumptions for the MCS model and the BS model as of November 1, 2016 and December 30, 2016, respectively, are as follows:

	November 1, 2016		December 30, 2016	
	Post-Closing Adjustment	Warrants	Warrants	
Fair market value of common stock	\$ 26.19	\$ 26.19	\$ 26.12	
Expected term	60 days	5 years	5 years	
Average risk-free rate of return	0.27%	1.31%	1.93%	
Expected volatility	33%	34%	33%	
Expected dividend yield	—%	—%	—%	

The Adjusted VWAP Price Per Share for the Post-Closing Adjustment and the exercise price of the Warrants are estimated based on simulated paths. Since we became a publicly traded company after the separation and did not have sufficient historical trading data to estimate the expected volatility, we estimated the expected volatility of our common stock based on the historical price volatility of the publicly traded shares of comparable companies in the same business as the Company over the periods equal to the expected term of these financial instruments. The risk-free interest rate was based on the U.S. Treasury zero-coupon yield in effect with maturity terms equal to the expected term of the financial instruments. The dividend yield was estimated to be zero.

Note 14 –Retirement Plans

Certain of the Company’s employees participate in noncontributory defined benefit plans and post-retirement medical plans sponsored by YUM prior to October 31, 2016. The Company has considered these plans to be part of multi-employer plans. YUM has allocated expenses related to our employees’ participation in our Consolidated and Combined Statements of Income. However, our Consolidated and Combined Balance Sheets do not reflect any assets or the liabilities related to these plans. We consider the expense allocation methodology and results to be reasonable for the periods prior to October 31, 2016. Subsequent to the separation, employees participating in YUM’s plans were enrolled in YCHLRP, as discussed below.

For executives who were hired or re-hired after September 30, 2001, YUM has implemented the YUM LRP. This is an unfunded, unsecured account-based retirement plan which allocates a percentage of pay to an account payable to the executive following the executive's separation of employment from YUM or attainment of age 55. The Company adopted the YCHLRP upon the separation, and YCHLRP will continue to be in effect until terminated by the Company's board of directors. The terms of the YCHLRP are substantially similar to the terms of the YUM LRP. Under the YCHLRP, certain executives who are at least age 21, who are classified as salary level 12, who are not eligible to participate in a tax-qualified defined benefit plan, and who satisfy certain additional requirements as to work location and assignment, are eligible to participate in the YCHLRP if selected for participation by the Company. The YCHLRP is an unfunded, unsecured account-based retirement plan that allocates a percentage of pay to an account payable to an executive following the later to occur of the executive's separation of employment from the Company or attainment of age 55. Under the YCHLRP, participants aged 55 or older are entitled to a lump sum distribution of their account balance on the last day of the calendar quarter that occurs on or follows their separation of employment. The liability of \$3.3 million and \$0.1 million attributable to our employees under the YUM LRP and YCHLRP, respectively, is included in our Consolidated and Combined Balance Sheets.

YUM offers certain of the Company's executives working in China retirement benefits under the Bai Sheng Restaurants (Hong Kong) Ltd. Retirement Scheme. Under this defined contribution plan, YUM provides a company funded contribution ranging from 5% to 10% of an executive's base salary. Upon termination, participants will receive a lump sum equal to a percentage of the Company's contributions inclusive of investment return. This percentage is based on a vesting schedule that provides participants with a vested 30% interest upon completion of a minimum of 3 years of service, and an additional 10% vested interest for each additional completed year, up to a maximum of 100%. The Company adopted the same plan after the separation and the contribution amount to the plan for the years ended December 31, 2016, 2015 and 2014 was insignificant.

As stipulated by Chinese state regulations, the Company participates in a government-sponsored defined contribution retirement plan. Substantially all employees are entitled to an annual pension equal to a fixed proportion of the average basic salary amount of the geographical area of their last employment at their retirement date. We are required to make contributions to the local social security bureau between 10% and 22% of the previous year's average basic salary amount of the geographical area where the employees are under our employment. Contributions are recorded in the Consolidated and Combined Statements of Income as they become payable. We have no obligation for the payment of pension benefits beyond the annual contributions as set out above. The Company contributed \$148 million, \$150 million and \$147 million to the government-sponsored plan for 2016, 2015 and 2014, respectively.

Note 15 – Share-Based Compensation

Overview

Prior to the separation, certain of the Company's employees were eligible to participate in YUM's Long-term Incentive Plan (the "YUM Plan"), pursuant to which they were granted awards of YUM common stock, including stock options, restricted stock units ("RSUs") and stock appreciation rights ("SARs"). YUM recognized stock-based compensation costs, net of estimated forfeitures, for only those shares expected to vest on a straight-line basis over the requisite service period of the award. Accordingly, certain costs related to the YUM Plan have been allocated to the Company and are reflected in the Consolidated and Combined Statements of Income in G&A expenses prior to the separation.

Upon the separation, holders of outstanding YUM equity awards generally received both adjusted YUM awards and Yum China awards, or adjusted awards of either YUM or Yum China in their entirety, to maintain the pre-separation intrinsic value of the awards. Depending on the tax laws of the country of employment, awards were modified using either the shareholder method or the employer method. Share issuances for Yum China awards held by YUM's employees will be satisfied by Yum China. Share issuances for YUM awards held by the Company's employees will be satisfied by YUM. The shareholder method was based on the premise that employees holding YUM awards prior to the separation should receive an equal number of awards of both YUM and Yum China. Under the employer method, employees holding YUM awards prior to the separation had their awards converted into awards of the company that they worked for subsequent to the separation. As a result, Yum China may issue shares of common stock to YUM's employees upon exercise or vesting of various types of awards, including stock options, SARs, RSUs, and awards from the executive income deferral plan.

The modified equity awards have the same terms and conditions as the awards held immediately before the separation, except that the number of shares and the price were adjusted. In accordance with ASC 718, the Company compared the fair value of the awards immediately prior to the separation to the fair value immediately after the separation to measure the incremental compensation cost, using the BS model. The incremental compensation cost was insignificant, and YUM and the Company continue to recognize the unamortized original grant-date fair value of the modified awards over the remaining requisite service period as their respective employees continue to provide services. Share-based compensation for the Company's employees is based on both YUM awards and Yum China awards held by those employees.

Effective October 31, 2016, the Company adopted the Yum China Holdings, Inc. Long Term Incentive Plan (the "2016 Plan"). The Company has reserved for issuance under the 2016 Plan of 45,000,000 shares of our common stock. Under this plan, the exercise price of stock options and SARs granted must be equal to or greater than the fair market value of the Company's stock on the date of grant.

Potential awards to employees and non-employee directors under the 2016 Plan include stock options, incentive options, SARs, restricted stock, stock units, RSUs, performance shares, performance units, and cash incentive awards. We have issued only stock options, SARs and RSUs under the 2016 Plan. While awards under the 2016 Plan can have varying vesting provisions and exercise periods, outstanding awards under the 2016 Plan vest in periods ranging from three to five years. Stock options and SARs expire ten years after grant. The Company recognizes all share-based payments to employees and non-employee directors in the Consolidated and Combined Financial Statements as compensation cost on a straight-line basis over the service period based on their fair value on the date of grant, for awards that actually vest. If no substantive service condition exists, the grant-date fair value is fully recognized as expense upon grant. Certain awards are subject to specific retirement conditions, which allow the awards to fully vest as long as the employee is actively employed for at least one year following the grant date, provides at least six months notification of intention to retire, and signs non-solicitation and non-compete agreements. Under such circumstances, the grant-date fair value of the award is recognized as expense on a straight-line basis over the one-year service period from the grant date.

Award Valuation

YUM and the Company estimated the fair value of each stock option and SAR award granted to the Company's employees as of the date of grant, using the BS model with the following assumptions:

	2016	2015	2014
Risk-free interest rate	1.3% - 1.4%	1.3%	1.6%
Expected term (years)	6.5 - 6.75	6.5	6.3
Expected volatility	27% - 35%	27.0%	29.9%
Expected dividend yield	0% - 2.6%	2.2%	2.1%

Awards granted to employees typically have a graded vesting schedule of 25% per year over four years and expire ten years after grant. Both YUM and the Company use a single weighted-average term for awards that have a graded vesting schedule. Based on analysis of the historical exercise and post-vesting termination behavior, YUM and the Company determined that employees exercised the awards on average after 6.5 years. Forfeitures were estimated based on historical experience. Historical data used to estimate the expected term and forfeiture rate were based on data associated with the Company's employees who were granted share-based awards by YUM prior to the separation.

For those awards granted by YUM prior to the separation, when determining expected volatility, YUM considered both historical volatility of its stock as well as implied volatility associated with its publicly traded options. The expected dividend yield is based on the annual dividend yield at the time of grant. For those awards granted by the Company after the separation, the Company considered the volatility of common shares of comparable companies in the same business as the Company. The Company had no plan to pay dividends at the time of the grant.

RSU awards generally vest over a three-year period, with certain awards vesting at 50% on the second grant anniversary and 50% on the third grant anniversary, and other awards vesting at 25%, 25% and 50% on each respective grant anniversary over the three-year period. The fair values of RSU awards are based on the closing price of YUM stock or the Company's stock on the date of grant.

On November 11, 2016, Yum China also granted annual awards of common stock to non-employee directors for their service on Yum China's board of directors. The fair value of these awards is based on the closing price per share of Yum China common stock on the date of grant. The shares were issued outright to the directors on the date of grant, with no conditions attached. Therefore, the fair value of the awards was fully recognized as expenses upon grant. For the year ended December 31, 2016, a total of 64,209 shares of Yum China common stock were granted to non-employee directors and the grant-date fair value of \$1.7 million was immediately recognized in full in the Consolidated and Combined Statements of Income.

Award Activity

Stock Options and SARs

	Shares (in thousands)	Weighted- Average Exercise Price	Weighted- Average Remaining Contractual Term (years)	Aggregate Intrinsic Value (in millions)
Outstanding at the beginning of the year	—	—		
Converted from YUM equity awards ^(a)	25,274	17.57		
Granted	500	26.98		
Exercised	(590)	9.99		
Forfeited or expired	(456)	21.13		
Outstanding at the end of the year	<u>24,728</u> ^(b)	<u>17.88</u>	5.94	204
Exercisable at the end of the year	<u>14,883</u>	<u>15.32</u>	4.36	161

- (a) Awards converted from YUM equity awards include 1,345,259 and 23,928,259 stock options and SARs held by the Company's employees (including non-employee directors of Yum China) and YUM's employees, respectively, as a result of the modification of YUM equity awards prior to the separation.

- (b) Outstanding awards include 1,335,131 stock options and 23,393,125 SARs with weighted average exercise prices of \$14.10 and \$18.09, respectively. Outstanding awards represent Yum China awards held by employees of both the Company and YUM.

The weighted-average grant-date fair value of SARs granted in 2016, 2015 and 2014 was \$12.78, \$16.11 and \$17.45, respectively. The total intrinsic value of stock options and SARs exercised by the Company's employees during the years ended December 31, 2016, 2015 and 2014, was \$25 million, \$33 million and \$16 million, respectively.

As of December 31, 2016, \$22 million of unrecognized compensation cost related to unvested stock options and SARs, which will be reduced by any forfeitures that occur, is expected to be recognized over a remaining weighted-average vesting period of approximately 1.77 years. This reflects unrecognized cost for both Yum China awards and YUM awards held by the Company's employees. The total fair value at grant date or modification date of awards held by the Company's employees that vested during 2016, 2015 and 2014 was \$11 million, \$6 million and \$7 million, respectively.

RSUs

	Shares (in thousands)	Weighted- Average Grant Date Fair Value
Unvested at the beginning of the year	—	—
Converted from YUM equity awards ^(a)	349	21.96
Granted	201	26.98
Vested	(2)	22.29
Forfeited or expired	(2)	22.57
Unvested at the end of the year	<u>546</u>	<u>23.81</u>

- (a) Awards converted from YUM equity awards include 226,445 and 122,830 RSUs held by the Company's employees (including non-employee directors of Yum China) and YUM's employees, respectively, as a result of modification of YUM equity awards prior to the separation.

As of December 31, 2016, there was \$8 million of unrecognized compensation cost related to 545,846 unvested RSUs.

Impact on Net Income

Share-based compensation expense was \$16 million, \$14 million and \$13 million for 2016, 2015 and 2014, respectively. Deferred tax benefits recognized totaled \$3 million in each of 2016, 2015 and 2014.

Note 16 – Equity

On September 23, 2016, YUM's board of directors approved the distribution of its shares of Yum China common stock to YUM's stockholders on a pro rata basis. On October 31, 2016, YUM's shareholders of record as of October 19, 2016 received one share of Yum China common stock for every one share of YUM's common stock held as of the record date. On October 31, 2016, we completed the legal separation from YUM, and we began trading "regular way" under the ticker symbol "YUMC" on the New York Stock Exchange on November 1, 2016. Following the separation, YUM does not own any equity interest in us.

Immediately after the separation on October 31, 2016, Yum China authorized capital stock consisted of 1,000,000,000 shares of common stock, par value \$0.01 per share, and 363,758,219 shares of Yum China common stock were issued and outstanding. As of December 31, 2016, 383,344,835.42 shares of Yum China common stock were issued and outstanding.

On October 27, 2016, a duly authorized committee of Yum China's board of directors adopted a stockholder rights plan (the "Rights Plan"), pursuant to which the board declared a dividend, to Yum China's sole stockholder of record as of October 27, 2016, of one preferred stock purchase right (a "Right") for each of share of Yum China common stock. The Rights will initially trade with, and will be inseparable from, Yum China common stock. The Rights Plan expires on October 27, 2017. New Rights will accompany any new shares of Yum China common stock issued until the Rights become exercisable or the Rights Plan expires. The original dividend of the Rights to the existing shareholder was recorded at fair value, which was insignificant given the contingent nature of the Rights. The embedded Rights are considered clearly and closely related to the underlying equity host and, therefore, do not require separate accounting.

Accumulated Other Comprehensive Income ("AOCI")

The Company's other comprehensive income (loss) for the years ended December 31, 2016, 2015, and 2014 and AOCI balances as of December 31, 2016 and 2015 were comprised solely of foreign currency translation adjustments. Other comprehensive loss was \$132 million, \$93 million, and \$52 million for the years ended December 31, 2016, 2015, and 2014, respectively. The accumulated balances reported in AOCI on the Consolidated and Combined Balance Sheets for currency translation adjustments were \$1 million and \$130 million as of December 31, 2016 and 2015, respectively. There was no tax effect related to the components of other comprehensive income for all years presented.

Restricted net assets

The Company's ability to pay dividends is primarily dependent on the Company receiving distributions of funds from its subsidiaries. Relevant PRC statutory laws and regulations permit payments of dividends by the Company's PRC subsidiaries only out of their retained earnings, if any, as determined in accordance with PRC accounting standards and regulations. The results of operations reflected in the Consolidated and Combined Financial Statements prepared in accordance with U.S. GAAP differ from those reflected in the statutory financial statements of the Company's subsidiaries.

In accordance with the PRC Regulations on Enterprises with Foreign Investment and the articles of association of the Company's PRC subsidiaries, a foreign-invested enterprise established in the PRC is required to provide certain statutory reserves, namely general reserve fund, the enterprise expansion fund and staff welfare and bonus fund which are appropriated from net profit as reported in the enterprise's PRC statutory accounts. A foreign-invested enterprise is required to allocate at least 10% of its annual after-tax profit to the general reserve until such reserve has reached 50% of its respective registered capital based on the enterprise's PRC statutory accounts. Appropriations to the enterprise expansion fund and staff welfare and bonus fund are at the discretion of the board of directors for all foreign-invested enterprises. The aforementioned reserves can only be used for specific purposes and are not distributable as cash dividends.

As a result of these PRC laws and regulations subject to the limit discussed above that require annual appropriations of 10% of after-tax income to be set aside, prior to payment of dividends as general reserve fund, the Company's PRC subsidiaries are restricted in their ability to transfer a portion of their net assets to the Company in the form of dividend payments, loans or advances. The restricted net assets of the PRC subsidiaries is approximately \$572 million as of December 31, 2016.

Furthermore, cash transfers from the Company's PRC subsidiaries to its subsidiaries outside of China are subject to PRC government control of currency conversion. Shortages in the availability of foreign currency may restrict the ability of the PRC subsidiaries to remit sufficient foreign currency to pay dividends or other payments to the Company, or otherwise satisfy their foreign currency denominated obligations.

Note 17 – Income Taxes

Prior to October 31, 2016, the Company's results have historically been included in the consolidated U.S. federal tax return and U.S. state income tax filings of YUM. Our foreign income tax returns, primarily those filed by our China subsidiaries, are filed on an individual entity basis. The Company has calculated its provision using the separate return method in these Consolidated and Combined Financial Statements. Under this method, the Company is assumed to have filed hypothetical tax returns on a standalone basis separate from YUM in the relevant tax jurisdictions. Any additional accrued tax liability attributable to the Company arising from the separate return method has been shown as settled against the net Parent Company Investment account in these Consolidated and Combined Financial Statements. The Company has recorded deferred taxes on its temporary differences, including hypothetical carryforwards and tax credits created by the separate tax return filings. The established current and deferred tax balances may not be indicative of the Company's actual balances prior to the separation.

Subsequent to October 31, 2016, the Company became a separate taxpayer and will prepare its own consolidated U.S. federal income tax return and U.S. state income tax filings. As of December 31, 2016, the current and deferred taxes, including carryforwards and tax credits, are reflective of the Company's actual balances subsequent to the separation.

U.S. and foreign income before taxes are set forth below:

	2016	2015	2014
U.S.	\$ 5	\$ (7)	\$ 15
China	659	502	—
Other Foreign	8	1	2
	<u>\$ 672</u>	<u>\$ 496</u>	<u>\$ 17</u>

The details of our income tax provision (benefit) are set forth below:

	2016	2015	2014
Current: Federal	\$ (2)	\$ 7	\$ 9
Foreign	200	132	149
	<u>\$ 198</u>	<u>\$ 139</u>	<u>\$ 158</u>
Deferred: Federal	\$ (36)	\$ (7)	\$ (9)
Foreign	(4)	36	(95)
	<u>\$ (40)</u>	<u>\$ 29</u>	<u>\$ (104)</u>
	<u>\$ 158</u>	<u>\$ 168</u>	<u>\$ 54</u>

The reconciliation of income taxes calculated at the U.S. federal statutory rate to our effective tax rate is set forth below:

	2016		2015		2014	
U.S. federal statutory rate	\$ 235	35.0%	\$ 173	35.0%	\$ 6	35.0%
Statutory rate differential attributable to foreign operations	(55)	(8.4)	(15)	(3.1)	5	32.2
Adjustments to reserves and prior years	16	2.4	3	0.6	(3)	(20.9)
Change in valuation allowances	—	—	12	2.4	13	79.8
Tax benefit from Little Sheep restructuring	(26)	(3.8)	—	—	—	—
Tax impact from Little Sheep goodwill impairment	—	—	—	—	40	240.8
Other, net	(12)	(1.7)	(5)	(1.0)	(7)	(44.6)
Effective income tax rate	<u>\$ 158</u>	<u>23.5%</u>	<u>\$ 168</u>	<u>33.9%</u>	<u>\$ 54</u>	<u>322.3%</u>

Statutory rate differential attributable to foreign operations. This item includes local taxes, withholding taxes, and shareholder-level taxes, net of foreign tax credits. The favorable impact is primarily attributable to a majority of our income being earned in China where it is subject to a 25% tax rate, which is lower than the U.S. federal statutory rate of 35%

In 2016, 2015 and 2014, this benefit was negatively impacted by the actual and deemed repatriation of current year foreign earnings to the U.S. as we recognized additional tax expense, resulting from the related effective tax rate being lower than the U.S. federal statutory rate.

Adjustments to reserves and prior years. This item includes: (1) changes in tax reserves, including interest thereon, established for potential exposure we may incur if a taxing authority takes a position on a matter contrary to our position; and (2) the effects of reconciling income tax amounts recorded in our Consolidated and Combined Statements of Income to amounts reflected on our tax returns, including any adjustments to the Consolidated and Combined Balance Sheets. The impact of certain effects or changes may offset items reflected in the ‘*Statutory rate differential attributable to foreign operations*’ line.

In 2016, this item was negatively impacted by the additional amount recorded for uncertain tax positions in China, whereas in 2014, it was favorably impacted by the resolution of uncertain tax positions in China.

Change in valuation allowances. This item relates to changes for deferred tax assets generated or utilized during the current year and changes in our judgment regarding the likelihood of using deferred tax assets that existed at the beginning of the year. The impact of certain changes may offset items reflected in the ‘*Statutory rate differential attributable to foreign operations*’ line.

In 2015 and 2014, \$12 million and \$13 million, respectively, of net tax expense was driven by valuation allowances recorded against deferred tax assets generated during the current year.

Tax benefit from Little Sheep restructuring. In 2016, we recognized tax benefit of \$26 million as a result of Little Sheep legal entity restructuring completed prior to the separation. The cash tax savings associated with this benefit will be realized as we recognize future U.S. taxable income.

Tax impact from Little Sheep goodwill impairment. In 2014, we recorded \$160 million of non-cash impairment of Little Sheep goodwill, which resulted in no related tax benefit. See Note 5.

Other. This item primarily includes the impact of permanent differences related to current year earnings as well as U.S. tax credits and deductions.

In 2016, this item was favorably impacted by non-taxable gain from changes in fair value of financial instruments associated with the Investors' strategic investment in Yum China. See Note 13.

The details of 2016 and 2015 deferred tax assets (liabilities) are set forth below:

	2016	2015
Operating losses and tax credit carryforwards	\$ 86	\$ 66
Tax benefit from Little Sheep restructuring	26	—
Employee benefits	4	2
Share-based compensation	8	11
Deferred escalating minimum rent	42	43
Various liabilities	8	14
Deferred income and other	35	37
Gross deferred tax assets	209	173
Deferred tax asset valuation allowances	(41)	(45)
Net deferred tax assets	\$ 168	\$ 128
Intangible assets	(22)	\$ (23)
Property, plant and equipment	(1)	(4)
Other	(9)	(9)
Gross deferred tax liabilities	\$ (32)	\$ (36)
Net deferred tax assets	\$ 136	\$ 92
Reported in Consolidated and Combined Balance Sheets as:		
Deferred income taxes	162	\$ 116
Other liabilities and deferred credits	(26)	(24)
	\$ 136	\$ 92

We have investments in our foreign subsidiaries where the carrying values for financial reporting exceed the tax basis. We have not provided deferred tax on the portion of the excess that we believe is indefinitely reinvested, as we have the ability and intent to indefinitely postpone the basis differences from reversing with a tax consequence. The Company's separation from YUM is intended to qualify as a tax-free reorganization for U.S. income tax purposes resulting in the excess of financial reporting basis over tax basis in our investment in the China business continuing to be indefinitely reinvested. This amount may become taxable upon an actual or deemed repatriation of assets from the subsidiaries or a sale or liquidation of the subsidiaries. We estimate that our total temporary difference upon which we have not provided deferred tax is approximately \$1.5 billion at December 31, 2016. However, it is not practicable to determine the deferred tax liability on this amount due to uncertainty with regard to the timing or manner of repatriation and the related impact on local taxes, withholding taxes and foreign tax credits.

At December 31, 2016, the Company has operating loss carryforwards of \$160 million, primarily related to our Little Sheep business, all of which will expire by 2021. These losses are being carried forward in jurisdictions where we are permitted to use tax losses from prior periods to reduce future taxable income.

As of December 31, 2016, the Company has U.S. tax credit carryforwards of \$46 million, which represents Yum China's foreign tax credit carryforwards as a result of the separation. This was attributable to the distributions from the Company's China business to YUM after Yum China was incorporated and became the parent of the Company's operating entities in China. The tax credits will expire by 2026.

At December 31, 2016, the Company also has tax benefit from Little Sheep restructuring of \$26 million, \$12 million and \$14 million of which will expire by 2026 and 2036, respectively.

Cash payments for tax liabilities on income tax returns filed in China were \$182 million, \$143 million and \$186 million in 2016, 2015 and 2014, respectively.

We recognize the benefit of positions taken or expected to be taken in tax returns in the financial statements when it is more likely than not that the position would be sustained upon examination by tax authorities. A recognized tax position is measured at the largest amount of benefit that is greater than fifty percent likely of being realized upon settlement.

A reconciliation of the beginning and ending amount of unrecognized tax benefits is as follows:

	2016	2015
Beginning of Year	\$ 15	\$ 13
Additions on tax positions	14	4
Reductions due to statute expiration	(3)	(2)
End of Year	<u>\$ 26</u>	<u>\$ 15</u>

In 2016 and 2015, we increased our unrecognized tax benefits by \$14 million and \$4 million, respectively, related to uncertainty with regard to the deductibility of certain business expenses incurred during the year. The Company believes it is reasonably possible its unrecognized tax benefits may decrease by approximately \$6 million in the next twelve months, all of which, if recognized upon audit settlement or statute expiration, would affect the 2017 effective tax rate.

The Company's results are subject to examination in the U.S. federal jurisdiction as well as various U.S. state jurisdictions as part of YUM's and our own income tax filings, and separately in foreign jurisdictions. Any liability arising from these examinations is expected to be settled among the Company, YCCL and YUM in accordance with the tax matters agreement we entered into in connection with the separation.

YUM has settled audits with the IRS through fiscal year 2010. The Company's operations in foreign jurisdictions generally remain subject to examination for tax years as far back as 2006, some of which years are currently under audit by local tax authorities. The accrued interest and penalties related to income taxes at December 31, 2016 and 2015 are set forth below:

	2016	2015
Accrued interest and penalties	\$ 5	\$ 3

During 2016, 2015 and 2014, a net expense of \$3 million, \$1 million and a net benefit of \$4 million, respectively, for interest and penalties was recognized in our Consolidated and Combined Statements of Income as components of our income tax provision.

Note 18 – Reportable Operating Segments

We have two reportable segments: KFC and Pizza Hut Casual Dining. We also have four non-reportable operating segments, Pizza Hut Home Service, East Dawning, Little Sheep and Taco Bell, which are combined and referred to as All Other Segments, as these operating segments are individually insignificant.

	Revenues		
	2016	2015	2014
KFC	\$ 4,696	\$ 4,768	\$ 4,893
Pizza Hut Casual Dining	1,774	1,825	1,696
All Other Segments	282	316	345
	<u>\$ 6,752</u>	<u>\$ 6,909</u>	<u>\$ 6,934</u>

	Operating Profit; Interest Income, Net; and Income Before Income Taxes		
	2016	2015	2014
KFC ^(a)	\$ 645	\$ 499	\$ 435
Pizza Hut Casual Dining	150	145	176
All Other Segments	(6)	(14)	(44)
Unallocated and corporate expenses ^(b)	(153)	(144)	(143)
Unallocated Closures and impairment expense ^{(b)(c)}	(17)	—	(463)
Unallocated Refranchising gain ^(b)	15	13	17
Unallocated Other income (expense) ^(b)	6	(11)	25
Operating Profit	<u>640</u>	<u>488</u>	<u>3</u>
Interest income, net ^(b)	11	8	14
Changes in fair value of financial instruments	21	—	—
Income Before Income Taxes	<u>\$ 672</u>	<u>\$ 496</u>	<u>\$ 17</u>

	Depreciation and Amortization		
	2016	2015	2014
KFC	\$ 266	\$ 283	\$ 286
Pizza Hut Casual Dining	111	109	92
All Other Segments	14	20	20
Corporate	11	13	13
	<u>\$ 402</u>	<u>\$ 425</u>	<u>\$ 411</u>

	Capital Spending		
	2016	2015	2014
KFC	\$ 221	\$ 259	\$ 269
Pizza Hut Casual Dining	118	176	187
All Other Segments	12	16	23
Corporate	85	61	46
	<u>\$ 436</u>	<u>\$ 512</u>	<u>\$ 525</u>

	Identifiable Assets	
	2016	2015
KFC ^(d)	\$ 1,411	\$ 1,577
Pizza Hut Casual Dining	628	718
All Other Segments	160	181
Corporate ^(e)	1,528	725
	<u>\$ 3,727</u>	<u>\$ 3,201</u>

	Long-Lived Assets ^(f)	
	2016	2015
KFC	\$ 1,099	\$ 1,248
Pizza Hut Casual Dining	553	616
All Other Segments	129	146
Corporate	33	23
	<u>\$ 1,814</u>	<u>\$ 2,033</u>

- (a) Includes equity income from investments in unconsolidated affiliates of \$54 million, \$41 million and \$30 million in 2016, 2015 and 2014, respectively.
- (b) Amounts have not been allocated to any segment for performance reporting purposes.
- (c) Represents 2014 impairment losses related to Little Sheep and 2016 incremental restaurant-level impairment charges. See Note 5.
- (d) Includes investments in 3 unconsolidated affiliates totaling \$71 million and \$61 for 2016 and 2015, respectively.
- (e) Primarily includes cash and inventories that are centrally managed.
- (f) Includes property, plant and equipment, net, goodwill, and intangible assets, net.

Note 19 – Contingencies

Indemnification of China Tax on Indirect Transfers of Assets

In February 2015, the Chinese State Administration of Taxation (“SAT”) issued Bulletin 7 on Income arising from Indirect Transfers of Assets by Non-Resident Enterprises. Pursuant to Bulletin 7, an “indirect transfer” of Chinese taxable assets, including equity interests in a Chinese resident enterprise (“Chinese interests”), by a non-resident enterprise, may be recharacterized and treated as a direct transfer of Chinese taxable assets, if such arrangement does not have reasonable commercial purpose and the transferor has avoided payment of Chinese enterprise income tax. As a result, gains derived from such an indirect transfer may be subject to Chinese enterprise income tax at a rate of 10%.

YUM concluded and we concurred that it is more likely than not that YUM will not be subject to this tax with respect to the distribution. However, given how recently Bulletin 7 was promulgated, there are significant uncertainties regarding what constitutes a reasonable commercial purpose, how the safe harbor provisions for group restructurings are to be interpreted and how the taxing authorities will ultimately view the distribution. As a result, YUM’s position could be challenged by Chinese tax authorities resulting in a 10% tax assessed on the difference between the fair market value and the tax basis of the separated China business. As YUM’s tax basis in the China business is minimal, the amount of such a tax could be significant.

Any tax liability arising from the application of Bulletin 7 to the distribution is expected to be settled in accordance with the tax matters agreement between the Company and YUM. Pursuant to the tax matters agreement, to the extent any Chinese indirect transfer tax pursuant to Bulletin 7 is imposed, such tax and related losses will be allocated between YUM and the Company in proportion to their respective share of the combined market capitalization of YUM and the Company during the thirty trading days after the separation. Such a settlement could be significant and have a material adverse effect on our results of operations and our financial condition. At the inception of the tax indemnity being provided to YUM, the fair value of the non-contingent obligation to stand ready to perform was insignificant and the liability for the contingent obligation to make payment was not probable or estimable.

Unconsolidated Affiliates Guarantees

From time to time we have guaranteed certain lines of credit and loans of unconsolidated affiliates. As of December 31, 2016, there are no guarantees outstanding for unconsolidated affiliates. Our unconsolidated affiliates had total revenues of approximately \$1,106 million for the year ended December 31, 2016 and assets and debt of approximately \$283 million and \$132 million, respectively, at December 31, 2016.

Indemnification of Officers and Directors

The Company's amended and restated certificate of incorporation and amended and restated bylaws include provisions that require the Company to indemnify directors or officers for monetary damages for actions taken as a director or officer of the Company or while serving at the Company's request as a director or officer or another position at another corporation or enterprise, as the case may be. The Company purchases standard directors and officers insurance to cover claims or a portion of the claims made against its directors and officers. Since a maximum obligation is not explicitly stated in the Company's bylaws or in the indemnification agreements and will depend on the facts and circumstances that arise out of any future claims, the overall maximum amount of the obligations cannot be reasonably estimated. The Company has not been required to make payments related to these obligations, and the fair value for these obligations is zero as of December 31, 2016.

Legal Proceedings

The Company is subject to various lawsuits covering a variety of allegations from time to time. The Company believes that the ultimate liability, if any, in excess of amounts already provided for these matters in the Consolidated and Combined Financial Statements, is not likely to have a material adverse effect on the Company's annual results of operations, financial condition or cash flows. Matters faced by the Company from time to time include, but are not limited to, claims from landlords, employees, customers and others related to operational, contractual or employment issues.

Note 20 – Selected Quarterly Financial Data (Unaudited)

	First Quarter	Second Quarter	2016 Third Quarter	Fourth Quarter	Total
Revenues:					
Company sales	\$ 1,278	\$ 1,558	\$ 1,848	\$ 1,938	\$ 6,622
Franchise fees and income	25	30	35	40	130
Total revenues	1,303	1,588	1,883	1,978	6,752
Restaurant profit	246	196	356	214	1,012
Operating Profit	209	87	286	58	640
Net Income – Yum China Holdings, Inc.	145	77	192	88	502
Basic earnings per common share	\$ 0.40	\$ 0.21	\$ 0.53	\$ 0.23	\$ 1.36
Diluted earnings per common share	\$ 0.40	\$ 0.21	\$ 0.53	\$ 0.23	\$ 1.36

	First Quarter	Second Quarter	2015 Third Quarter	Fourth Quarter	Total
Revenues:					
Company sales	\$ 1,235	\$ 1,608	\$ 1,935	\$ 2,011	\$ 6,789
Franchise fees and income	21	28	34	37	120
Total revenues	1,256	1,636	1,969	2,048	6,909
Restaurant profit	192	185	318	163	858
Operating Profit	142	86	255	5	488
Net Income – Yum China Holdings, Inc.	101	64	187	(29)	323
Basic earnings (losses) per common share	\$ 0.28	\$ 0.18	\$ 0.51	\$ (0.08)	\$ 0.89
Diluted earnings (losses) per common share	\$ 0.28	\$ 0.18	\$ 0.51	\$ (0.08)	\$ 0.89

Note 21 – Subsequent EventsSegments

In the first quarter of 2017, we started discussions on integrating the management and business approach for Pizza Hut Casual Dining and Pizza Hut Home Service which allows us to create a network of approximately 2,000 stores for pizza delivery. As we make progress on implementing changes, we will continue to evaluate the impact on reportable segments.

Share Repurchase Program

On February 7, 2017, we announced that our board of directors authorized a \$300 million share repurchase program. Yum China may repurchase shares under this program from time to time in open market or privately negotiated transactions, including block trades, accelerated share repurchase transactions and Rule 10b5-1 trading plans.

Share-Based Compensation

On February 10, 2017, the Company's board of directors approved grants of 87,972 RSUs and 2,230,544 SARs to the employees under the 2016 Plan. The estimated total grant-date fair value of these awards is \$25 million, which will be recognized on a straight-line basis over the vesting periods.

On February 28, 2017, the Company's board of directors approved a grant of 75 RSUs to each eligible RGM under the 2016 Plan. The estimated total grant-date fair value of these awards is approximately \$12 million, which will be recognized on a straight-line basis over the vesting periods.

Item 9. Changes In and Disagreements with Accountants on Accounting and Financial Disclosure.

None.

Item 9A. Controls and Procedures.

Evaluation of Disclosure Controls and Procedures

The Company has evaluated the effectiveness of the design and operation of its disclosure controls and procedures pursuant to Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934 as of the end of the period covered by this report. Based on the evaluation, performed under the supervision and with the participation of the Company's management, including the Chief Executive Officer (the "CEO") and the Chief Financial Officer (the "CFO"), the Company's management, including the CEO and CFO, concluded that the Company's disclosure controls and procedures were effective as of the end of the period covered by this report.

Internal Controls Over Financial Reporting

Under the rules and regulations of the SEC, the Company is not required to comply with the requirements of Section 404 of the Sarbanes-Oxley Act of 2002 until its Annual Report on Form 10-K for the year ended December 31, 2017 and this annual report does not include a report of management's assessment regarding internal control over financial reporting or an attestation report of the Company's independent registered public accounting firm. In its Annual Report on Form 10-K for the year ended December 31, 2017, management will be required to report on the effectiveness of the Company's internal control over financial reporting and the Company's independent registered public accounting firm will be required to provide a report on its audit of the effectiveness of the Company's internal control over financial reporting.

Changes in Internal Control

There were no changes with respect to the Company's internal control over financial reporting or in other factors that materially affected, or are reasonably likely to materially affect, internal control over financial reporting during the quarter ended December 31, 2016.

Item 9B. Other Information.

None.

PART III

Item 10. Directors, Executive Officers and Corporate Governance.

Information regarding Section 16(a) compliance, the Company's Audit Committee and the Audit Committee financial expert, the Company's code of ethics and background of the directors appearing under the captions "Stock Ownership Information," "Governance of the Company," "Executive Compensation" and "Item 1: Election of Directors" is incorporated herein by reference to the 2017 Proxy Statement.

Information regarding executive officers of the Company is incorporated by reference from Part I of this Form 10-K.

Item 11. Executive Compensation.

Information regarding executive and director compensation and the Company's Compensation Committee appearing under the captions "Governance of the Company" and "Executive Compensation" is incorporated herein by reference to the 2017 Proxy Statement.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.

Information regarding equity compensation plans and security ownership of certain beneficial owners and management appearing under the captions "Executive Compensation" and "Stock Ownership Information" is incorporated herein by reference to the 2017 Proxy Statement.

Item 13. Certain Relationships and Related Transactions, and Director Independence.

Information regarding certain relationships and related transactions and information regarding director independence appearing under the caption "Governance of the Company" and "Item 1: Election of Directors" is incorporated herein by reference to the 2017 Proxy Statement.

Item 14. Principal Accountant Fees and Services.

Information regarding principal accountant fees and services and audit committee pre-approval policies and procedures appearing under the caption "Item 2: Ratification of Independent Auditor" is incorporated herein by reference to the 2017 Proxy Statement.

PART IV

Item 15. Exhibits and Financial Statement Schedules.

- (a) (1) Financial Statements: Consolidated and Combined Financial Statements filed as part of this report are listed under Part II, Item 8 of this Form 10-K.
- (2) Financial Statement Schedules: No schedules are required because either the required information is not present or not present in amounts sufficient to require submission of the schedule, or because the information required is included in the Consolidated and Combined Financial Statements thereto filed as a part of this Form 10-K.
- (3) Exhibits: The exhibits listed in the accompanying Exhibit Index are filed as part of this Form 10-K. The Index to Exhibits specifically identifies each management contract or compensatory plan required to be filed as an exhibit to this Form 10-K.

Item 16. Form 10-K Summary.

Not applicable.

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.

YUM CHINA HOLDINGS, INC.

By: /s/ Micky Pant

Micky Pant

Chief Executive Officer

Date: March 8, 2017

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

<u>Signature</u>	<u>Title</u>	<u>Date</u>
<u>/s/ Micky Pant</u> Micky Pant	Chief Executive Officer and Director (principal executive officer)	March 8, 2017
<u>/s/ Ted Stedem</u> Ted Stedem	Chief Financial Officer (principal financial officer)	March 8, 2017
<u>/s/ Paul Hill</u> Paul Hill	Vice President and Controller (principal accounting officer)	March 8, 2017
<u>/s/ Peter A. Bassi</u> Peter A. Bassi	Director	March 8, 2017
<u>/s/ Christian L. Campbell</u> Christian L. Campbell	Director	March 8, 2017
<u>/s/ Ed Yiu-Cheong Chan</u> Ed Yiu-Cheong Chan	Director	March 8, 2017
<u>/s/ Edouard Ettedgui</u> Edouard Ettedgui	Director	March 8, 2017
<u>/s/ Louis T. Hsieh</u> Louis T. Hsieh	Director	March 8, 2017
<u>/s/ Fred Hu</u> Fred Hu	Director	March 8, 2017
<u>/s/ Jonathan S. Linen</u> Jonathan S. Linen	Director	March 8, 2017
<u>/s/ Ruby Lu</u> Ruby Lu	Director	March 8, 2017
<u>/s/ Zili Shao</u> Zili Shao	Director	March 8, 2017

Yum China Holdings, Inc.
Exhibit Index
(Item 15)

<u>Exhibit Number</u>	<u>Description of Exhibits</u>
2.1**	Separation and Distribution Agreement, dated as of October 31, 2016, by and among Yum! Brands, Inc, Yum Restaurants Consulting (Shanghai) Company Limited and Yum China Holdings, Inc. (incorporated by reference to Exhibit 2.1 to Yum China Holdings, Inc.'s Current Report on Form 8-K filed on November 1, 2016).
3.1	Amended and Restated Certificate of Incorporation of Yum China Holdings, Inc. (incorporated by reference to Exhibit 3.1 to Yum China Holdings, Inc.'s Current Report on Form 8-K filed on November 1, 2016).
3.2	Amended and Restated Bylaws of Yum China Holdings, Inc. (incorporated by reference to Exhibit 3.2 to Yum China Holdings, Inc.'s Current Report on Form 8-K filed on November 1, 2016).
3.3	Certificate of Designations of Preferred Stock (incorporated by reference to Exhibit 3.1 to Yum China Holdings, Inc.'s Registration Statement on Form 8-A filed on October 27, 2016).
4.1	Rights Agreement, dated as of October 27, 2016, by and between Yum China Holdings, Inc. and American Stock Transfer & Trust Company, LLC as rights agent (incorporated by reference to Exhibit 4.1 to Yum China Holdings, Inc.'s Registration Statement on Form 8-A filed on October 27, 2016).
4.2	Warrant No. 1 issued to Pollos Investment L.P. on January 9, 2017 (incorporated by reference to Exhibit 10.3 to Yum China Holdings, Inc.'s Current Report on Form 8-K filed on January 9, 2017).
4.3	Warrant No. 2 issued to Pollos Investment L.P. on January 9, 2017 (incorporated by reference to Exhibit 10.4 to Yum China Holdings, Inc.'s Current Report on Form 8-K filed on January 9, 2017).
4.4	Warrant No. 1 issued to API (Hong Kong) Investment Limited on January 9, 2017 (incorporated by reference to Exhibit 10.5 to Yum China Holdings, Inc.'s Current Report on Form 8-K filed on January 9, 2017).
4.5	Warrant No. 2 issued to API (Hong Kong) Investment Limited on January 9, 2017 (incorporated by reference to Exhibit 10.6 to Yum China Holdings, Inc.'s Current Report on Form 8-K filed on January 9, 2017).
10.1	Master License Agreement, dated as of October 31, 2016, by and between Yum! Restaurants Asia Pte. Ltd. and Yum Restaurants Consulting (Shanghai) Company Limited (incorporated by reference to Exhibit 10.1 to Yum China Holdings, Inc.'s Current Report on Form 8-K filed on November 1, 2016).
10.2	Tax Matters Agreement, dated as of October 31, 2016, by and among Yum! Brands, Inc., Yum China Holdings, Inc. and Yum Restaurants Consulting (Shanghai) Company Limited (incorporated by reference to Exhibit 10.2 to Yum China Holdings, Inc.'s Current Report on Form 8-K filed on November 1, 2016).

**Exhibit
Number**

Description of Exhibits

- 10.3 Employee Matters Agreement, dated as of October 31, 2016, by and between Yum! Brands, Inc. and Yum China Holdings, Inc. (incorporated by reference to Exhibit 10.3 to Yum China Holdings, Inc.'s Current Report on Form 8-K filed on November 1, 2016).
- 10.4 Transition Services Agreement, dated as of October 31, 2016, by and between Yum! Brands, Inc. and Yum China Holdings, Inc. (incorporated by reference to Exhibit 10.4 to Yum China Holdings, Inc.'s Current Report on Form 8-K filed on November 1, 2016).
- 10.5 Name License Agreement, dated as of October 31, 2016, by and between Yum! Brands, Inc. and Yum China Holdings, Inc. (incorporated by reference to Exhibit 10.5 to Yum China Holdings, Inc.'s Current Report on Form 8-K filed on November 1, 2016).
- 10.6 Guaranty of Master License Agreement, dated as of October 31, 2016, by Yum China Holdings, Inc. (incorporated by reference to Exhibit 10.6 to Yum China Holdings, Inc.'s Current Report on Form 8-K filed on November 1, 2016).
- 10.7 Investment Agreement, dated as of September 1, 2016, by and among Yum! Brands, Inc., Yum China Holdings, Inc. and Pollos Investment L.P. (incorporated by reference to Exhibit 10.11 to Amendment No. 5 to Yum China Holdings, Inc.'s Registration Statement on Form 10, filed on September 16, 2016).
- 10.8 Investment Agreement, dated as of September 1, 2016, by and among Yum! Brands, Inc., Yum China Holdings, Inc. and API (Hong Kong) Investment Limited (incorporated by reference to Exhibit 10.12 to Amendment No. 5 to Yum China Holdings, Inc.'s Registration Statement on Form 10, filed on September 16, 2016).
- 10.9 Letter Agreement, dated as of October 7, 2016, by and among Yum! Brands, Inc., Yum China Holdings, Inc., API (Hong Kong) Investment Limited and Pollos Investment L.P. *
- 10.10 Shareholders Agreement, dated as of November 1, 2016, by and among Yum China Holdings, Inc., Pollos Investment L.P. and API (Hong Kong) Investment Limited (incorporated by reference to Exhibit 10.7 to Yum China Holdings, Inc.'s Current Report on Form 8-K filed on November 1, 2016).
- 10.11 Form of Yum China Holdings, Inc. Indemnification Agreement, (incorporated by reference to Exhibit 10.10 to Yum China Holdings, Inc.'s Current Report on Form 8-K filed on November 1, 2016).
- 10.12 Letter of Understanding, dated as of October 28, 2016, by and between Yum China Holdings, Inc. and Micky Pant (incorporated by reference to Exhibit 10.11 to Yum China Holdings, Inc.'s Current Report on Form 8-K filed on November 1, 2016). †
- 10.13 Yum China Holdings, Inc. Long Term Incentive Plan (incorporated by reference to Exhibit 10.7 to Amendment No. 5 to Yum China Holdings, Inc.'s Registration Statement on Form 10, filed on September 16, 2016). †
- 10.14 Yum China Holdings, Inc. Leadership Retirement Plan (incorporated by reference to Exhibit 10.8 to Amendment No. 5 to Yum China Holdings, Inc.'s Registration Statement on Form 10, filed on September 16, 2016). †

<u>Exhibit Number</u>	<u>Description of Exhibits</u>
10.15	Form of Restricted Stock Unit Agreement (incorporated by reference to Exhibit 10.10 to Amendment No. 5 to Yum China Holdings, Inc.'s Registration Statement on Form 10, filed on September 16, 2016). †
10.16	Form of Stock Appreciation Right Agreement (incorporated by reference to Exhibit 10.9 to Amendment No. 5 to Yum China Holdings, Inc.'s Registration Statement on Form 10, filed on September 16, 2016). †
10.17	Letter of Understanding between Yum! Restaurants Consulting (Shanghai) Company Limited and Ted Stedem, dated as of August 3, 2016 (incorporated by reference to Exhibit 10.14 to Amendment No. 7 to Yum China Holdings, Inc.'s Registration Statement on Form 10, filed on October 6, 2016). †
10.18	Letter of Understanding between Yum! Restaurants Consulting (Shanghai) Company Limited and Joey Wat, dated as of March 21, 2014.*, †
10.19	Letter of Understanding issued by Yum! Restaurants Consulting (Shanghai) Company Limited to Joey Wat, dated as of September 8, 2015.*, †
10.20	Letter of Understanding issued by Yum China Holdings, Inc. to Joey Wat, dated as of February 6, 2017.*, †
10.21	Letter of Understanding issued by Yum China Holdings, Inc. to Johnson Huang, dated as of February 6, 2017.*, †
10.22	Letter of Understanding issued by Yum China Holdings, Inc. to Mark Chu, dated as of February 6, 2017.*, †
21.1	Subsidiaries of Yum China Holdings, Inc.*
23.1	Consent of Independent Registered Public Accounting Firm.*
31.1	Certification of the Chief Executive Officer pursuant to Rule 13a-14(a) of Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.*
31.2	Certification of the Chief Financial Officer pursuant to Rule 13a-14(a) of Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.*
32.1	Certification of the Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.*
32.2	Certification of the Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.*
101.INS	XBRL Instance Document *
101.SCH	XBRL Taxonomy Extension Schema Document *
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document *

**Exhibit
Number**

Description of Exhibits

- 101.LAB XBRL Taxonomy Extension Label Linkbase Document *
- 101.PRE XBRL Taxonomy Extension Presentation Linkbase Document *
- 101.DEF XBRL Taxonomy Extension Definition Linkbase Document *

* Filed or furnished herewith.

** Certain schedules and exhibits to this agreement have been omitted in accordance with Item 601(b)(2) of Regulation S-K. A copy of any omitted schedules and/or exhibits will be furnished to the Securities and Exchange Commission upon request.

† Indicates a management contract or compensatory plan.

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YumChina