

AMAZON COM INC
Form 10-Q
April 26, 2019
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2019

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 No. 000-22513

AMAZON.COM, INC.

(Exact name of registrant as specified in its charter)

Delaware 91-1646860

(State or other jurisdiction of (I.R.S. Employer
incorporation or organization) Identification No.)

410 Terry Avenue North, Seattle, Washington 98109-5210
(206) 266-1000

(Address and telephone number, including area code, of registrant's principal executive offices)

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 every Interactive Data File required to be submitted 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 such files). Yes No

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

Large accelerated filer Accelerated filer

Non-accelerated filer Smaller reporting company

Emerging growth company

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

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

492,331,776 shares of common stock, par value \$0.01 per share, outstanding as of April 17, 2019

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AMAZON.COM, INC.

FORM 10-Q

For the Quarterly Period Ended March 31, 2019

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

AMAZON.COM, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(in millions)

(unaudited)

	Three Months Ended March 31,		Twelve Months Ended March 31,	
	2018	2019	2018	2019
CASH, CASH EQUIVALENTS, AND RESTRICTED CASH, BEGINNING OF PERIOD	\$21,856	\$32,173	\$16,301	\$17,616
OPERATING ACTIVITIES:				
Net income	1,629	3,561	3,938	12,005
Adjustments to reconcile net income to net cash from operating activities:				
Depreciation and amortization of property and equipment and capitalized content costs, operating lease assets, and other	3,671	4,854	12,714	16,524
Stock-based compensation	1,182	1,274	4,605	5,509
Other operating expense (income), net	56	(13)	216	205
Other expense (income), net	(184)	(135)	(437)	268
Deferred income taxes	141	415	134	714
Changes in operating assets and liabilities:				
Inventories	2,220	719	(2,309)	(2,815)
Accounts receivable, net and other	1,029	(401)	(4,716)	(6,043)
Accounts payable	(10,216)	(6,384)	3,749	7,095
Accrued expenses and other	(2,225)	(2,932)	(538)	(235)
Unearned revenue	906	888	838	1,133
Net cash provided by (used in) operating activities	(1,791)	1,846	18,194	34,360
INVESTING ACTIVITIES:				
Purchases of property and equipment	(3,098)	(3,290)	(12,905)	(13,619)
Proceeds from property and equipment incentives	371	569	1,981	2,303
Acquisitions, net of cash acquired, and other	(13)	(1,169)	(13,939)	(3,342)
Sales and maturities of marketable securities	2,677	2,643	10,444	8,205
Purchases of marketable securities	(470)	(6,876)	(11,846)	(13,506)
Net cash provided by (used in) investing activities	(533)	(8,123)	(26,265)	(19,959)
FINANCING ACTIVITIES:				
Proceeds from long-term debt and other	125	190	16,332	833
Repayments of long-term debt and other	(202)	(351)	(1,463)	(817)
Principal repayments of finance leases	(2,015)	(2,214)	(5,981)	(7,649)
Principal repayments of financing obligations	(72)	(2)	(235)	(266)
Net cash provided by (used in) financing activities	(2,164)	(2,377)	8,653	(7,899)
Foreign currency effect on cash, cash equivalents, and restricted cash	248	(12)	733	(611)
Net increase (decrease) in cash, cash equivalents, and restricted cash	(4,240)	(8,666)	1,315	5,891
CASH, CASH EQUIVALENTS, AND RESTRICTED CASH, END OF PERIOD	\$17,616	\$23,507	\$17,616	\$23,507
SUPPLEMENTAL CASH FLOW INFORMATION:				
Cash paid for interest on long-term debt	\$282	\$286	\$607	\$858
Cash paid for operating leases	—	709	—	709

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Cash paid for interest on finance leases	75	165	234	471
Cash paid for interest on financing obligations	54	2	153	142
Cash paid for income taxes, net of refunds	513	168	1,224	840
Assets acquired under operating leases	—	875	—	875
Property and equipment acquired under finance leases	2,270	2,628	10,020	10,972
Property and equipment acquired under build-to-suit arrangements	741	436	3,081	3,336
See accompanying notes to consolidated financial statements.				

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AMAZON.COM, INC.
 CONSOLIDATED STATEMENTS OF OPERATIONS
 (in millions, except per share data)
 (unaudited)

	Three Months Ended March 31,	
	2018	2019
Net product sales	\$31,605	\$34,283
Net service sales	19,437	25,417
Total net sales	51,042	59,700
Operating expenses:		
Cost of sales	30,735	33,920
Fulfillment	7,792	8,601
Marketing	2,699	3,664
Technology and content	6,759	7,927
General and administrative	1,067	1,173
Other operating expense (income), net	63	(5)
Total operating expenses	49,115	55,280
Operating income	1,927	4,420
Interest income	80	183
Interest expense	(330)	(366)
Other income (expense), net	239	164
Total non-operating income (expense)	(11)	(19)
Income before income taxes	1,916	4,401
Provision for income taxes	(287)	(836)
Equity-method investment activity, net of tax	—	(4)
Net income	\$1,629	\$3,561
Basic earnings per share	\$3.36	\$7.24
Diluted earnings per share	\$3.27	\$7.09
Weighted-average shares used in computation of earnings per share:		
Basic	484	491
Diluted	498	502

See accompanying notes to consolidated financial statements.

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AMAZON.COM, INC.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(in millions)

(unaudited)

	Three Months Ended March 31,	
	2018	2019
Net income	\$1,629	\$3,561
Other comprehensive income (loss):		
Foreign currency translation adjustments, net of tax of \$21 and \$(1)	59	(8)
Net change in unrealized gains (losses) on available-for-sale debt securities:		
Unrealized gains (losses), net of tax of \$9 and \$0	(44)	32
Reclassification adjustment for losses (gains) included in "Other income (expense), net," net of tax of \$0 and \$0	2	1
Net unrealized gains (losses) on available-for-sale debt securities	(42)	33
Total other comprehensive income (loss)	17	25
Comprehensive income	\$1,646	\$3,586
See accompanying notes to consolidated financial statements.		

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AMAZON.COM, INC.
CONSOLIDATED BALANCE SHEETS
(in millions, except per share data)

	December 31, 2018	March 31, 2019 (unaudited)
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 31,750	\$ 23,115
Marketable securities	9,500	13,905
Inventories	17,174	16,432
Accounts receivable, net and other	16,677	15,979
Total current assets	75,101	69,431
Property and equipment, net	61,797	61,048
Operating leases	—	20,132
Goodwill	14,548	14,708
Other assets	11,202	12,783
Total assets	\$ 162,648	\$ 178,102
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 38,192	\$ 31,809
Accrued expenses and other	23,663	24,588
Unearned revenue	6,536	7,298
Total current liabilities	68,391	63,695
Long-term lease liabilities	9,650	33,275
Long-term debt	23,495	23,322
Other long-term liabilities	17,563	9,400
Commitments and contingencies (Note 4)		
Stockholders' equity:		
Preferred stock, \$0.01 par value:		
Authorized shares — 500		
Issued and outstanding shares — none	—	—
Common stock, \$0.01 par value:		
Authorized shares — 5,000		
Issued shares — 514 and 516		
Outstanding shares — 491 and 492	5	5
Treasury stock, at cost	(1,837) (1,837)
Additional paid-in capital	26,791	28,059
Accumulated other comprehensive loss	(1,035) (1,010)
Retained earnings	19,625	23,193
Total stockholders' equity	43,549	48,410
Total liabilities and stockholders' equity	\$ 162,648	\$ 178,102

See accompanying notes to consolidated financial statements.

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AMAZON.COM, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

Note 1 — ACCOUNTING POLICIES

Unaudited Interim Financial Information

We have prepared the accompanying consolidated financial statements pursuant to the rules and regulations of the Securities and Exchange Commission (the “SEC”) for interim financial reporting. These consolidated financial statements are unaudited and, in our opinion, include all adjustments, consisting of normal recurring adjustments and accruals necessary for a fair presentation of our consolidated balance sheets, operating results, and cash flows for the periods presented. Operating results for the periods presented are not necessarily indicative of the results that may be expected for 2019 due to seasonal and other factors. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States (“GAAP”) have been omitted in accordance with the rules and regulations of the SEC. These consolidated financial statements should be read in conjunction with the audited consolidated financial statements and accompanying notes in Item 8 of Part II, “Financial Statements and Supplementary Data,” of our 2018 Annual Report on Form 10-K.

Prior Period Reclassifications

Certain prior period amounts have been reclassified to conform to the current period presentation, including the reclassification of long-term capital lease obligations that existed at December 31, 2018 from “Other long-term liabilities” to “Long-term lease liabilities” within the consolidated balance sheets, as a result of the adoption of new accounting guidance for leases. See “Accounting Pronouncements Recently Adopted.”

Principles of Consolidation

The consolidated financial statements include the accounts of Amazon.com, Inc., its wholly-owned subsidiaries, and those entities in which we have a variable interest and of which we are the primary beneficiary, including certain entities in India and China and that support our seller lending financing activities (collectively, the “Company”). Intercompany balances and transactions between consolidated entities are eliminated.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires estimates and assumptions that affect the reported amounts of assets and liabilities, revenues and expenses, and related disclosures of contingent liabilities in the consolidated financial statements and accompanying notes. Estimates are used for, but not limited to, income taxes, commitments and contingencies, valuation of acquired intangibles and goodwill, stock-based compensation forfeiture rates, vendor funding, and inventory valuation. Actual results could differ materially from those estimates.

Earnings per Share

Basic earnings per share is calculated using our weighted-average outstanding common shares. Diluted earnings per share is calculated using our weighted-average outstanding common shares including the dilutive effect of stock awards as determined under the treasury stock method. In periods when we have a net loss, stock awards are excluded from our calculation of earnings per share as their inclusion would have an antidilutive effect.

The following table shows the calculation of diluted shares (in millions):

	Three	
	Months	
	Ended	
	March	
	31,	
	2018	2019
Shares used in computation of basic earnings per share	484	491
Total dilutive effect of outstanding stock awards	14	11
Shares used in computation of diluted earnings per share	498	502
Accounts Receivable, Net and Other		

Included in “Accounts receivable, net and other” on our consolidated balance sheets are amounts primarily related to customers, vendors, and sellers. As of December 31, 2018 and March 31, 2019, customer receivables, net, were \$9.4 billion and \$9.8 billion, vendor receivables, net, were \$3.2 billion and \$2.5 billion, and seller receivables, net, were \$710 million and \$660 million. Seller receivables are amounts due from sellers related to our seller lending program, which provides funding to sellers primarily to procure inventory.

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Leases

We categorize leases with contractual terms longer than twelve months as either operating or finance. Finance leases are generally those leases that allow us to substantially utilize or pay for the entire asset over its estimated life. Assets acquired under finance leases are recorded in property and equipment, net. All other leases are categorized as operating leases. Our leases generally have terms that range from two to ten years for equipment and two to twenty years for property.

Certain lease contracts include obligations to pay for other services, such as operations and maintenance. For leases of property, we account for these other services as a component of the lease. For substantially all other leases, the services are accounted for separately and we allocate payments to the lease and other services components based on estimated stand-alone prices.

Lease liabilities are recognized at the present value of the fixed lease payments, reduced by landlord incentives using a discount rate based on similarly secured borrowings available to us. Lease assets are recognized based on the initial present value of the fixed lease payments, reduced by landlord incentives, plus any direct costs from executing the leases. Lease assets are tested for impairment in the same manner as long-lived assets used in operations. Leasehold improvements are capitalized at cost and amortized over the lesser of their expected useful life or the lease term. When we have the option to extend the lease term, terminate the lease before the contractual expiration date, or purchase the leased asset, and it is reasonably certain that we will exercise the option, we consider these options in determining the classification and measurement of the lease. Our leases may include variable payments based on measures that include changes in price indices, market interest rates, or the level of sales at a physical store, which are expensed as incurred.

Costs associated with operating lease assets are recognized on a straight-line basis within operating expenses over the term of the lease. Finance lease assets are amortized within operating expenses on a straight-line basis over the shorter of the estimated useful lives of the assets or the lease term. The interest component of a finance lease is included in interest expense and recognized using the effective interest method over the lease term.

Financing Obligations

We record assets and liabilities for estimated construction costs under build-to-suit lease arrangements when we have control over the building during the construction period. If we continue to control the building after the construction period, the arrangement is classified as a financing obligation instead of a lease. The building is depreciated over the shorter of its useful life or the term of the obligation.

If we do not control the building after the construction period ends, the assets and liabilities for construction costs are derecognized, and we classify the lease as either operating or finance.

Digital Video and Music Content

We obtain video content, inclusive of episodic television and movies, and music content for customers through licensing agreements that have a wide range of licensing provisions including both fixed and variable payment schedules. When the license fee for a specific video or music title is determinable or reasonably estimable and the content is available to us, we recognize an asset and a corresponding liability for the amounts owed. We reduce the liability as payments are made and we amortize the asset to “Cost of sales” on an accelerated basis, based on estimated usage or viewing patterns, or on a straight-line basis. If the licensing fee is not determinable or reasonably estimable, no asset or liability is recorded and licensing costs are expensed as incurred. We also develop original video content for which the production costs are capitalized and amortized to “Cost of sales” predominantly on an accelerated basis that follows the viewing patterns associated with the content. The weighted average remaining life of our capitalized video content is 2.6 years.

Our produced and licensed video content is primarily monetized together as a unit, referred to as a film group, in each major geography where we offer Amazon Prime memberships. These film groups are evaluated for impairment whenever an event occurs or circumstances change indicating the fair value is less than the carrying value. The total capitalized costs of video, which is primarily released content, and music as of December 31, 2018 and March 31, 2019 were \$3.8 billion and \$4.2 billion. Total video and music expense was \$1.5 billion and \$1.7 billion in Q1 2018 and Q1 2019. Total video and music expense includes licensing and production costs associated with content offered within Amazon Prime memberships, and costs associated with digital subscriptions and sold or rented content.

Unearned Revenue

Unearned revenue is recorded when payments are received or due in advance of performing our service obligations and is recognized over the service period. Unearned revenue primarily relates to prepayments of AWS services and Amazon Prime memberships. Our total unearned revenue as of December 31, 2018 was \$7.9 billion, of which \$2.8 billion was recognized as revenue during the three months ended March 31, 2019. Included in “Other long-term liabilities” on our consolidated balance sheets was \$1.4 billion of unearned revenue as of December 31, 2018 and March 31, 2019.

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Additionally, we have performance obligations, primarily related to AWS, associated with commitments in customer contracts for future services that have not yet been recognized in our financial statements. For contracts with original terms that exceed one year, those commitments not yet recognized were \$21.6 billion as of March 31, 2019. The weighted average remaining life of our long-term contracts is 3.3 years. However, the amount and timing of revenue recognition is largely driven by customer usage, which can extend beyond the original contractual term.

Accounting Pronouncements Recently Adopted

In February 2016, the Financial Accounting Standards Board (“FASB”) issued an Accounting Standards Update (“ASU”) amending the accounting for leases, primarily requiring the recognition of lease assets and liabilities for operating leases with terms of more than twelve months on our consolidated balance sheets. Under the new guidance, leases previously described as capital lease obligations and finance lease obligations are now referred to as finance leases and financing obligations, respectively. We adopted this ASU on January 1, 2019 by recording an immaterial cumulative adjustment to retained earnings rather than retrospectively adjusting prior periods. Prior period amounts were not adjusted and continue to be reported in accordance with our historic accounting policies resulting in a balance sheet presentation that is not comparable to the prior period in the first year of adoption. The adoption of this ASU resulted in the recognition of operating lease assets and liabilities of approximately \$21 billion, which included the reclassification of finance lease obligations to operating leases of \$1.2 billion. As of December 31, 2018, amounts related to finance lease obligations and construction liabilities totaled \$9.6 billion, of which \$1.5 billion was derecognized for buildings that we do not control during the construction period and \$5.4 billion and \$1.5 billion were reclassified to finance leases and operating leases, respectively.

In March 2019, the FASB issued an ASU amending the accounting for film costs, inclusive of episodic television and movie costs. The new guidance aligns the accounting for production costs of episodic television with that of movies by requiring production costs to be capitalized. Previously, we only capitalized a portion of the production costs related to our produced episodic television content. We adopted this ASU as of January 1, 2019 and began capitalizing substantially all of our production costs. Adoption of this ASU resulted in approximately \$130 million of incremental capitalized film costs classified in “Other Assets” for the period ended March 31, 2019.

Note 2 — FINANCIAL INSTRUMENTSCash, Cash Equivalents, Restricted Cash, and Marketable Securities

As of December 31, 2018 and March 31, 2019, our cash, cash equivalents, restricted cash, and marketable securities primarily consisted of cash, AAA-rated money market funds, U.S. and foreign government and agency securities, and other investment grade securities. Cash equivalents and marketable securities are recorded at fair value. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. To increase the comparability of fair value measures, the following hierarchy prioritizes the inputs to valuation methodologies used to measure fair value:

Level 1—Valuations based on quoted prices for identical assets and liabilities in active markets.

Level 2—Valuations based on observable inputs other than quoted prices included in Level 1, such as quoted prices for similar assets and liabilities in active markets, quoted prices for identical or similar assets and liabilities in markets that are not active, or other inputs that are observable or can be corroborated by observable market data.

Level 3—Valuations based on unobservable inputs reflecting our own assumptions, consistent with reasonably available assumptions made by other market participants. These valuations require significant judgment.

We measure the fair value of money market funds and certain marketable equity securities based on quoted prices in active markets for identical assets or liabilities. Other marketable securities were valued either based on recent trades of securities in inactive markets or based on quoted market prices of similar instruments and other significant inputs derived from or corroborated by observable market data. We did not hold any cash, cash equivalents, restricted cash, or marketable securities categorized as Level 3 assets as of December 31, 2018 and March 31, 2019.

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The following table summarizes, by major security type, our cash, cash equivalents, restricted cash, and marketable securities that are measured at fair value on a recurring basis and are categorized using the fair value hierarchy (in millions):

	December 31, 2018		March 31, 2019		Total Estimated Fair Value
	Total Estimated Fair Value	Cost or Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	
Cash	\$ 10,406	\$ 8,635	\$ —	\$ —	\$ 8,635
Level 1 securities:					
Money market funds	12,515	9,515	—	—	9,515
Equity securities (1)	170				263
Level 2 securities:					
Foreign government and agency securities	815	1,382	—	—	1,382
U.S. government and agency securities	11,667	8,864	3	(13)	8,854
Corporate debt securities	4,990	7,396	8	(6)	7,398
Asset-backed securities	892	1,166	3	(2)	1,167
Other fixed income securities	188	201	—	(1)	200
Equity securities (1)	33				—
	\$ 41,676	\$ 37,159	\$ 14	\$ (22)	\$ 37,414
Less: Restricted cash, cash equivalents, and marketable securities (2)	(426)				(394)
Total cash, cash equivalents, and marketable securities	\$ 41,250				\$ 37,020

(1) The related unrealized gain (loss) recorded in “Other income (expense), net” was \$68 million in Q1 2019.

We are required to pledge or otherwise restrict a portion of our cash, cash equivalents, and marketable securities as collateral for real estate leases, amounts due to third-party sellers in certain jurisdictions, debt, and standby and (2) trade letters of credit. We classify cash, cash equivalents, and marketable securities with use restrictions of less than twelve months as “Accounts receivable, net and other” and of twelve months or longer as non-current “Other assets” on our consolidated balance sheets. See “Note 4 — Commitments and Contingencies.”

The following table summarizes the remaining contractual maturities of our cash equivalents and marketable fixed income securities as of March 31, 2019 (in millions):

	Amortized Cost	Estimated Fair Value
Due within one year	\$ 23,482	\$ 23,478
Due after one year through five years	4,274	4,277
Due after five years through ten years	190	190
Due after ten years	578	571
Total	\$ 28,524	\$ 28,516

Actual maturities may differ from the contractual maturities because borrowers may have certain prepayment conditions.

Equity Warrants and Non-Marketable Equity Securities

We hold equity warrants giving us the right to acquire stock of other companies. As of December 31, 2018 and March 31, 2019, these warrants had a fair value of \$440 million and \$594 million, and are recorded within “Other assets” on our consolidated balance sheets. The related gain (loss) recorded in “Other income (expense), net” was \$45 million and \$89 million in Q1 2018 and Q1 2019. These assets are primarily classified as Level 2 assets.

As of December 31, 2018 and March 31, 2019, equity securities not accounted for under the equity method and without readily determinable fair values, had a carrying value of \$282 million and \$888 million.

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Consolidated Statements of Cash Flows Reconciliation

The following table provides a reconciliation of the amount of cash, cash equivalents, and restricted cash reported within the consolidated balance sheets to the total of the same such amounts shown in the consolidated statements of cash flows (in millions):

	December 31, 2018	March 31, 2019
Cash and cash equivalents	\$ 31,750	\$ 23,115
Restricted cash included in accounts receivable, net and other	418	359
Restricted cash included in other assets	5	33
Total cash, cash equivalents, and restricted cash shown in the consolidated statements of cash flows	\$ 32,173	\$ 23,507

Note 3 — LEASES

Gross assets recorded under finance leases, included in “Property and equipment, net,” were \$36.1 billion and \$46.5 billion as of December 31, 2018 and March 31, 2019. Accumulated amortization associated with finance leases was \$19.8 billion and \$23.0 billion as of December 31, 2018 and March 31, 2019.

Lease cost recognized in our consolidated statements of operations is summarized as follows (in millions):

	Three Months Ended March 31, 2019
Operating lease cost (1)	\$ 836
Finance lease cost:	
Amortization of lease assets	2,307
Interest on lease liabilities	156
Finance lease cost	2,463
Variable lease cost	250
Total lease cost	\$ 3,549

(1) Rental expense under operating lease agreements was \$791 million for Q1 2018.

Other information about lease amounts recognized in our consolidated financial statements is summarized as follows:

	March 31, 2019
Weighted-average remaining lease term – operating leases	11.4 years
Weighted-average remaining lease term – finance leases	5.7 years
Weighted-average discount rate – operating leases	3.2 %
Weighted-average discount rate – finance leases	2.9 %

As of March 31, 2019, our lease liabilities were as follows (in millions):

	Operating Leases	Finance Leases	Total
Gross lease liabilities	\$ 26,731	\$ 25,004	\$ 51,735
Less: imputed interest			