

MCDONALDS CORP  
Form DEF 14A  
April 06, 2005  
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**SCHEDULE 14A INFORMATION**

**Proxy Statement Pursuant to Section 14(a) of the Securities Exchange Act of 1934 (Amendment No. )**

Filed by the Registrant

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Definitive Proxy Statement

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**McDonald s Corporation**

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**To McDonald's Corporation Shareholders:**

McDonald's Corporation will hold its 2005 Annual Shareholders Meeting on Wednesday, May 11, 2005, at 9:00 a.m. Central Time, in the Prairie Ballroom at The Lodge at McDonald's Office Campus, Oak Brook, Illinois. The registration desk will open at 7:30 a.m.

At the meeting, shareholders will be asked to:

1. Elect five Directors;
2. Approve the appointment of an independent registered public accounting firm to serve as independent auditors for 2005;
3. Act on a shareholder proposal, if presented; and
4. Transact other business properly presented at the meeting.

Shareholders are cordially invited to attend the Annual Shareholders Meeting. If you are unable to attend the meeting in person, you may watch a live webcast by going to [www.investor.mcdonalds.com](http://www.investor.mcdonalds.com) and clicking Webcast. A replay of the Annual Shareholders Meeting will be available for a limited time.

**Your Board of Directors recommends that you vote FOR all nominees for Director, FOR the approval of the independent auditors, and AGAINST the shareholder proposal. Your vote is important.**

Please consider the issues presented in this Proxy Statement and vote your shares as promptly as possible. This Notice of the Annual Shareholders Meeting and Proxy Statement and proxy or voting instruction card are being sent to shareholders beginning on or about April 6, 2005.

By order of the Board of Directors,

Gloria Santona  
Secretary

Oak Brook, Illinois

April 6, 2005

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### **Corporate Governance Principles and Board Matters**

#### **Corporate Governance**

The Sarbanes-Oxley Act of 2002 ushered in renewed focus on corporate governance among public companies in the United States, and the sub-headings in the following discussion respond to the specific disclosure requirements of the Securities and Exchange Commission (SEC) in this area. At McDonald's, however, we believe that good governance is more than a collection of regulations. It is the intersection of the relationships among our Board, our management and our shareholders and is informed by the values that have been the foundation of our business since its inception—integrity, fairness, diligence and ethical behavior.

Our Corporate Governance Principles are the center of our governance practices at McDonald's, and we have attached them as Appendix A to this Proxy Statement. They address matters that we believe are fundamental to ensuring that the interests of our shareholders are paramount, while taking appropriate account of other important constituencies, such as our employees and franchisees. For example, our Board of Directors must have a substantial majority of independent members—a standard that exceeds the New York Stock Exchange (NYSE) listing standards—and our Director nomination process continually strives to identify persons who have the initiative, time and skills that will permit them to make a meaningful contribution to the Board's oversight of the execution of our business plans. Our Corporate Governance Principles also impose limits on the outside activities of our Directors and require them to adhere to a specific code of conduct, so that McDonald's can have confidence in their commitment to the success of our operations. To underscore this commitment, our independent Directors receive equity-based compensation as part of their fees, and we require that they maintain a specified level of equity investment in McDonald's throughout their tenure.

Our Chairman of the Board, an independent Director, presides over regular executive sessions of the independent Directors, which promote a spirit of candid and constructive evaluation of management, the Company's strategy and competitive and other exposures over both short- and long-term horizons, among other matters. A key focus of these discussions is the development of appropriate management resources to meet our business needs, as well as unexpected personnel losses, such as those faced recently with the passing of our colleagues, Jim Cantalupo and Charlie Bell.

The Board's oversight is also effected through six standing committees. They are the Audit, Compensation, Governance, Finance, Corporate Responsibility and Executive Committees. Each of them operates under a written charter, which we believe ensures accountability among Committee members for their particular responsibilities.

The most important of our Board Committees—the Audit, Compensation and Governance Committees—are required by SEC regulations or NYSE listing standards, although McDonald's governance structure included these Committees long before the advent of these requirements. Each of these Committees performs important substantive and oversight functions, which are described in more detail below, and they work in a coordinated fashion to address recurring matters of legal and operational significance, as well as to respond to unanticipated events. The Audit Committee is responsible for oversight of financial reporting, internal controls and compliance. Among its principal functions is the selection of McDonald's independent auditors, which is subject to shareholder approval at our annual meetings, and the evaluation of our auditors' independence and performance. Given the importance of its responsibilities, the Audit Committee is also a critical player in setting the right tone at the top at McDonald's. In this role, it reviews complaints we receive about accounting or control matters and the appropriateness and terms of related-party transactions, among other matters, that may place our reputation or legal compliance at risk. The Committee's report on activities during 2004 is included on page 24.

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The Compensation Committee reviews compensation levels for officers throughout the Company, but has special responsibility for establishing goals and compensation levels for our Chief Executive Officer and other key executives. Its report on executive compensation at McDonald's is included on page 12 and should be read together with our other disclosures about the compensation and benefits of our most highly compensated officers.

The Governance Committee monitors our Board structure and operations. Among its most important functions is the identification, evaluation and recruitment of Director candidates, whether they are suggested by other Directors, management or our shareholders. The Committee makes a formal recommendation to the Board with respect to all proposed Director nominees, including those you will vote on this year.

While not mandated by law, our other Board Committees figure prominently in our vision of corporate governance, which we believe also includes responsible corporate citizenship. In 2000, the Board established its Corporate Responsibility Committee to address many of the social, health and environmental issues that confront companies in the restaurant and food industries—issues that we acknowledge resonate with shareholders, employees and customers alike. While good governance is only one part of the answer to these issues, we believe that dedicating our senior resources to them will advance a constructive debate and foster winning solutions.

McDonald's is proud of its governance structure and believes that governance is a journey, not a destination. For this reason, we review our Corporate Governance Principles annually, and our Board and its Committees engage in a self-evaluation and a review of their respective operations with a view to continuous improvement. Shareholders also are invited to communicate with us about these matters, and we provide information about how to do so on page 6 of this Proxy Statement. McDonald's has long believed

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that good corporate governance is critical to fulfilling the Company's obligation to shareholders we have been, and will remain, a leader in adopting sound practices for the oversight and execution of our business plans.

### **Director Independence**

Our Corporate Governance Principles require that a substantial majority of our Board members be independent. The Board has adopted categorical standards to assist it in making its independence determinations. A copy of our Standards on Director Independence is attached as Appendix B. Based on these standards and after reviewing any relationships involving Board members, including those described under Certain Relationships and Related Transactions on page 23, the Board determined that none of its non-management Directors has a material relationship with the Company, and therefore all of these Directors are independent. They are Hall Adams, Jr., Edward A. Brennan, Robert A. Eckert, Enrique Hernandez, Jr., Jeanne P. Jackson, Walter E. Massey, Andrew J. McKenna, Cary D. McMillan, John W. Rogers, Jr., Anne-Marie Slaughter and Roger W. Stone.

### **Financial Experts, Audit Committee Independence and Financial Literacy**

The Board of Directors determined that Enrique Hernandez, Jr., Cary D. McMillan and Roger W. Stone qualify as audit committee financial experts and that each member of the Audit Committee is independent and financially literate, all within the meaning of applicable rules of the SEC and the listing standards of the NYSE.

### **Board Committees**

*Our Corporate Governance Principles provide for six standing committees: Audit, Compensation, Governance, Finance, Corporate Responsibility and Executive. Charters for each of the key committees Audit, Compensation and Governance are attached as Appendices C, D and E, respectively. These charters, along with the charters for the Corporate Responsibility Committee and the Finance Committee, are available on the Company's website at [www.governance.mcdonalds.com](http://www.governance.mcdonalds.com).*

The **Audit Committee** appoints the Company's independent auditors and evaluates their independence and performance. The Audit Committee reviews with the internal auditors and the independent auditors the overall scope and results of their respective audits, the internal accounting and financial controls, and the steps management has taken to monitor and control the Company's major risk exposures. The Audit Committee also reviews the Company's material financial disclosures and pre-approves all audit and permitted non-audit services. In addition, the Audit Committee annually reviews the adequacy and appropriateness of the Company's compliance programs including the Company's disclosure controls and procedures. Members of the Committee are Directors Hernandez (Chairperson), Massey, McMillan and Stone. All members of the Audit Committee are independent within the meaning of the listing standards of the NYSE. In 2004, the Audit Committee met nine times, including meetings to review the Company's annual and quarterly financial results prior to their public issuance.

*The Audit Committee Report, a discussion of the Policy on the Pre-Approval of Audit and Permitted Non-Audit Services and a Summary of Auditor Fees and Services can be found on pages 24 and 25.*

The **Compensation Committee** evaluates the performance of the Company's Chief Executive Officer and approves his compensation in consultation with the non-management Directors; and based on recommendations from management, reviews and approves senior management's compensation and approves compensation guidelines for all other officers. The Committee administers the Company's incentive and equity compensation plans and, in consultation with senior management, reviews and approves compensation policies. Members of the Committee are Directors Brennan (Chairperson), Adams, Eckert, Jackson, Rogers and Slaughter. All members of the Compensation Committee are independent within the meaning of the listing standards of the NYSE. In 2004, the Compensation Committee met eight times. *The Compensation Committee Report on Executive Compensation can be found beginning on page 12.*

The **Governance Committee** sets criteria for Board membership; searches for and screens candidates to fill Board vacancies; recommends appropriate candidates for election each year and, in this regard, evaluates individual Director performance; assesses overall Board performance; considers Board composition and size; recommends to the Board the compensation paid to outside Directors; and evaluates the Company's corporate governance process. Members of the Committee are Directors McKenna (Chairperson), Brennan, Eckert, Hernandez and Stone. All members of the Governance Committee are independent within the meaning of the listing standards of the NYSE. In 2004, the Committee met six times.

The **Corporate Responsibility Committee** acts in an advisory capacity to the Company's management with respect to policies and strategies that affect the Company's role as a socially responsible organization, including issues pertaining to health and safety, the environment, employee opportunities, consumers and the communities in which the Company does business. Members of the Committee are Directors Massey (Chairperson), Adams, Rogers and Slaughter. In 2004, the Committee met twice.

The **Finance Committee** has principal oversight responsibility with respect to certain material financial matters that are outside the purview of the Audit Committee, including the Company's treasury activities as well as acquisitions and divestitures that are material to the Company's business. This Committee annually reviews the Company's worldwide insurance program, banking and trading arrangements, and policies with respect to dividends and share repurchase. Members of the Committee are Directors Jackson (Chairperson), McKenna, McMillan and Stone. The Committee met twice in 2004.

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The **Executive Committee** may exercise most Board powers during the period between Board meetings. Members of this Committee are Directors Skinner (Chairperson), Brennan, Hernandez, and McKenna. In 2004, the Committee met once.

**Board Compensation**

The Corporate Governance Principles provide that the Governance Committee recommends to the Board the form and amount of compensation for non-management Directors. Directors who are Company employees receive no compensation for their services as Directors. The following table shows McDonald's compensation for non-employee Directors for 2004 and planned compensation for 2005:

	<u>2004</u>	<u>2005</u>
Annual retainer	\$ 50,000	\$ 60,000
Attendance fees (per meeting):		
Board meeting	1,000	1,000
Committee meeting or executive session not held in conjunction with a Board meeting	1,000	1,000
Committee chairperson retainers:		
Audit, Compensation and Governance Committees	20,000	20,000
Corporate Responsibility and Finance Committees	10,000	10,000
Credit to Directors' Stock Plan account (a)	30,000	60,000
Stock option grants (number of shares)(b):		
Annual grant	5,000	0
Grant upon joining the Board	5,000	0
Matching gifts (aggregate maximum dollars matched per year)	10,000	10,000
Reimbursement for expenses attendant to Board membership	yes	yes

A special grant of 10,000 restricted stock units was made in 2004 to Mr. McKenna in recognition of his election as Chairman. These restricted stock units will vest on the later of one year from the grant date, July 15, 2004, or Mr. McKenna's retirement date. He also participates in the Board compensation described above.

- (a) Directors can defer their retainer and fees in the form of common stock equivalents under the Directors' Stock Plan. Deferred amounts are credited to an account that is adjusted to reflect dividends as well as gains or losses, as if invested in McDonald's common stock. Each outside Director who served for the entire year also received a credit of \$30,000 on December 31, 2004 (\$60,000 in 2005) to his or her Directors' Stock Plan account. Director Slaughter who served for a part of the year received a pro rata credit to her account. Deferred amounts are paid in cash after the Director retires from the Board or can be deferred further up to a maximum of 15 years at the option of the Director.
- (b) In May 2004, each outside Director received an option to purchase 5,000 shares of McDonald's common stock. The options vest in annual installments over three years, have a 10-year life and permit the holder to purchase shares at their fair market value on the grant date. Since 1995, a stock option grant was made to each outside Director when he or she joined the Board. We made a grant of this size to Anne-Marie Slaughter when she joined the Board in May 2004. Consistent with the advice of an outside compensation consultant, the Board approved the elimination of stock option grants as part of our Director compensation package, effective January 2005.

**Board and Committee Evaluations**

In accordance with our Corporate Governance Principles, the Governance Committee conducts annual evaluations of the Board of Directors. Individual Directors are evaluated periodically, but no less often than each time they are slated for re-election. In addition, the Audit, Compensation, Corporate Responsibility, Finance and Governance Committees each conducts self-evaluations and discusses the results of their respective evaluations at Committee meetings and with the full Board.

**Board Attendance at Annual Shareholders Meetings and Board and Committee Meetings**

Our Corporate Governance Principles provide that Directors are expected to attend the Company's Annual Shareholders Meeting, and all or substantially all Board meetings and meetings of the Committees on which they serve. From time to time, unforeseen circumstances may prevent a Director from attending. Over the past five years, all Directors have attended every Annual Shareholders Meeting. During this same period, the Directors held 48 Board meetings and a total of 136 Committee meetings. On average, Director attendance at these meetings exceeded 96%. In 2004, the Board met 13 times.

**Code of Conduct for the Board of Directors**

Each year, the Directors confirm that they have read the Code and will comply with its standards. *Our Code of Conduct for the Board of Directors is attached as Appendix F.*

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### **Director Selection Process**

The Company has a policy with regard to the consideration of Director candidates. Under the policy, the Governance Committee establishes criteria for Director nominees, screens candidates and recommends Director nominees who are approved by the full Board.

The Governance Committee considers candidates suggested by its members, other Directors, senior management and shareholders in anticipation of upcoming elections and actual or expected Board vacancies. The Committee may, at the Company's expense, retain search firms, consultants and other advisors to identify, screen and/or evaluate candidates.

All candidates, including those recommended by shareholders, are evaluated on the same basis in light of all of their credentials and the needs of the Board and the Company. Of particular importance are the candidate's integrity and judgment, professional achievements and experience relevant to the Company's business and strategic challenges, his or her potential contribution to the diversity and culture of the Board, and ability and willingness to devote sufficient time to Board duties. Candidates also are evaluated in light of Board policies, such as those relating to Director independence, tenure and service on other boards. Candidates with appropriate qualifications are interviewed in person, typically by the Chairman, the Chief Executive Officer, a majority of the members of the Governance Committee, and other available Directors.

The Governance Committee also evaluates sitting Directors whose terms are nearing expiration and who are being considered for renomination in light of the above considerations and their past contributions to the Board. *Shareholders who wish to nominate Director candidates should follow the procedures described in the section on Consideration of Director Nominations which can be found on page 6 of this Proxy Statement.*

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### **Communications**

#### **Shareholder Communications with the Board of Directors and Non-Management Directors**

Interested persons wishing to communicate directly with the Board or the non-management Directors, individually or as a group, may do so by sending written communications addressed to them at McDonald's Corporation, P.O. Box 4837, Oak Brook, IL 60522-4837. Under the Board's policy for communications addressed to the Board, the Company's Secretary collects mail from the Directors' post office box, forwards correspondence directed to an individual Director to that Director and screens correspondence directed to multiple Directors or the full Board in order to forward it to the most appropriate Committee chairperson, the Chairman or the full Board.

Communications to the Board, the non-management Directors or to any individual Director that relate to the Company's accounting, internal accounting controls or auditing matters are referred to the Chairperson of the Audit Committee.

#### **Consideration of Director Nominations**

Shareholders can suggest Director candidates for consideration by writing to the Governance Committee, c/o The Secretary, McDonald's Corporation, McDonald's Plaza, Oak Brook, IL 60523. Shareholders should provide the candidate's name, biographical data, qualifications and the candidate's written consent to being named as a nominee in the Company's Proxy Statement and to serve as a Director, if elected.

The Company's By-Laws provide that for Director nominations to be properly brought before an annual meeting by a shareholder, timely notice must be given by the shareholder to the Company's Secretary. To be timely, the notice must be delivered to the Secretary at the above address not less than 90 days nor more than 120 days before the one-year anniversary of the preceding year's annual meeting. With respect to the 2006 Annual Shareholders' Meeting, notice will be timely if it is delivered between January 20, 2006 and February 18, 2006.

#### **Shareholder Proposals for Inclusion in Next Year's Proxy Statement**

To be considered for inclusion in next year's Proxy Statement, shareholder proposals must be received by the Company's Secretary no later than December 9, 2005. These proposals should be sent to the Secretary by fax at 630-623-0497 or by mail to The Secretary, McDonald's Corporation, McDonald's Plaza, Oak Brook, IL 60523. This notice requirement is separate from and in addition to the SEC's requirements that a shareholder must meet in order to have a shareholder proposal included in the Company's Proxy Statement.

#### **Other Shareholder Proposals for Presentation at the 2006 Annual Shareholders' Meeting**

For any proposal that is not submitted for inclusion in next year's Proxy Statement, but is instead sought to be presented directly from the floor of the 2006 Annual Shareholders' Meeting, the Company's By-Laws require that timely notice must be given to the Company's Secretary. To be

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timely, the notice must be delivered to the Secretary at the above address between January 20, 2006 and February 18, 2006. The By-Laws also provide that the proposal, as determined by the Chairman of the meeting, must be a proper subject for shareholder action under Delaware corporation law.

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**Proposals to be Voted On**

***Proposal No. 1. Election of Directors***

The Board is divided into three classes, each having three-year terms that expire in successive years.

**Nominees**

**The nominees for Director are: Hall Adams, Jr., Cary D. McMillan, Michael J. Roberts, James A. Skinner and Anne-Marie Slaughter.**

Four of the nominees are standing for election as Directors at this year's Annual Shareholders Meeting to hold office for three-year terms expiring in 2008. These four are Hall Adams, Jr., Cary D. McMillan, James A. Skinner and Anne-Marie Slaughter. The fifth nominee, Michael J. Roberts, is standing for election in the class of 2007.

The Board of Directors expects all nominees to be available for election. If any of them should become unavailable to serve as a Director for any reason prior to the Annual Shareholders Meeting, the Board may substitute another person as a nominee. In that case, your shares will be voted for that other person.

Your shares will be voted according to your instructions. If you return your signed proxy card but do not provide voting instructions, your shares will be voted FOR the election of the five nominees named above. The five nominees who receive the most votes will be elected. Biographical information for the Directors continuing in office and the five nominees follows.

*The Board of Directors recommends that shareholders vote FOR all five nominees.*

**Biographical information**

**Hall Adams, Jr. Nominee.** Mr. Adams, 71, was the Chief Executive Officer of Leo Burnett & Co., Inc., an advertising firm, from 1987 until his retirement in 1992. Mr. Adams has served as a Director of McDonald's since 1993 and is nominated for the class of 2008. If elected, Mr. Adams would be expected to retire as a member of the Board of Directors at the 2007 Annual Shareholders Meeting in accordance with our Corporate Governance Principles.

**Edward A. Brennan** Mr. Brennan, 71, is the retired Chairman, President and Chief Executive Officer of Sears, Roebuck and Co., a merchandising company. He retired from Sears in 1995. From April 2003 to May 2004, Mr. Brennan served as Executive Chairman of AMR



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Corporation, the parent company of American Airlines, and Executive Chairman of American Airlines, Inc., a scheduled passenger airline and scheduled air freight carrier. Mr. Brennan joined McDonald's Board in 2002 and is a member of the class of 2007. He also serves on the boards of The Allstate Corporation, AMR Corporation, Exelon Corporation, Morgan Stanley and 3M Company.

**Robert A. Eckert** Mr. Eckert is Chairman and Chief Executive Officer of Mattel, Inc., a designer, manufacturer and marketer of family products, a post he has held since May 2000. Prior to joining Mattel, Mr. Eckert was President and Chief Executive Officer of Kraft Foods from 1997 to 2000. He joined the Board of McDonald's in 2003 and serves in the class of 2006. He is 50 years old.

**Enrique Hernandez, Jr.** Mr. Hernandez, 49, is Chairman and Chief Executive Officer of Inter-Con Security Systems, Inc., a provider of high-end security and facility support services to government, utilities and industrial customers, since 1986. He joined the Board in 1996 and serves in the class of 2006. Mr. Hernandez also serves as the lead director of Nordstrom, Inc., and as a director of Tribune Company and Wells Fargo & Company.

**Jeanne P. Jackson** Ms. Jackson, 53, is the General Partner of MSP Capital, a consulting and investment firm she founded in January 2003. Ms. Jackson was Chief Executive Officer of Walmart.com from March 2000 to January 2002. She formerly served as President and Chief Executive Officer of Banana Republic, a Gap Inc. brand, from July 1995 to March 2000, and held additional responsibilities for Gap Inc.'s Direct Division from November 1998 to March 2000. Ms. Jackson joined McDonald's Board in 1999 and is a member of the class of 2006. She also serves on the boards of NIKE, Inc., Nordstrom, Inc. and Williams-Sonoma, Inc.

**Walter E. Massey** Dr. Massey, 66, is President of Morehouse College, a post to which he was named in 1995. He serves as a director of Bank of America Corporation, BP p.l.c. and Motorola, Inc. Dr. Massey joined McDonald's Board in 1998 and is a member of the class of 2007.

**Andrew J. McKenna** Mr. McKenna, 75, is the Chairman of Schwarz Paper Company, a printer, converter, producer and distributor of packaging and promotional materials. Mr. McKenna is the presiding Director of the Board and in April 2004, he was elected Chairman of the Board. He joined McDonald's Board in 1991 and serves in the class of 2006. He is also a director of Aon Corporation, Click Commerce, Inc. and Skyline Corporation.

**Cary D. McMillan** *Nominee.* Mr. McMillan, 47, was the Chief Executive Officer of Sara Lee Branded Apparel from October 2001 to May 2004, and Executive Vice President, from January 2000 to May 2004, of Sara Lee Corporation, a branded consumer packaged goods company. From 1999 to 2001, Mr. McMillan was Chief Financial and Administrative Officer of Sara Lee Corporation. Prior to that time, he was Managing Partner of the Chicago office of Arthur Andersen, LLP. Mr. McMillan joined McDonald's Board in 2003 and is a nominee for the class of 2008. He also serves on the board of Hewitt Associates, Inc.

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**Michael J. Roberts Nominee.** Mr. Roberts, 54, is President and Chief Operating Officer, a post to which he was elected in November 2004, and also has served as a Director since that date. Previously, he was Chief Executive Officer McDonald's USA from July 2004 to November 2004 and prior to that, President McDonald's USA from June 2001. From July 1997 to June 2001, Mr. Roberts was President, West Division McDonald's USA. Mr. Roberts has been with the Company for 27 years and is nominated for the class of 2007.

**John W. Rogers, Jr.** Mr. Rogers is the Chairman and Chief Executive Officer of Ariel Capital Management, LLC, a privately held institutional money management firm and mutual fund company which he founded in 1983. Mr. Rogers, 47, joined the McDonald's Board in 2003 and serves in the class of 2007. Mr. Rogers is also a director of Aon Corporation, Bally Total Fitness Holding Corporation and Exelon Corporation, and a trustee of Ariel Investment Trust.

**James A. Skinner Nominee.** Mr. Skinner, 60, is Vice Chairman and Chief Executive Officer, a post to which he was elected in November 2004, and also has served as a Director since that date. He served as Vice Chairman from January 2003 to November 2004 and as President and Chief Operating Officer of McDonald's Restaurant Group from February 2002 to December 2002. Prior to that, he served as President and Chief Operating Officer of McDonald's Europe, Asia/Pacific, Middle East and Africa from June 2001 to February 2002; and President of McDonald's Europe from December 1997 to June 2001. Mr. Skinner has been with the Company for 34 years and is a nominee for the class of 2008.

**Anne-Marie Slaughter Nominee.** For the past three years, Dr. Slaughter has been the Dean of the Woodrow Wilson School of Public and International Affairs, Princeton University. From 1994 to 2002, she was the Director of Graduate and International Studies at Harvard Law School, and the J. Sinclair Armstrong Professor of International, Foreign and Comparative Law. Dr. Slaughter, 46, joined the Board in 2004 and is a nominee for the class of 2008.

**Roger W. Stone** Mr. Stone is Manager of Stone-Kaplan Investments, LLC, a private investment company, since July 2004. He was Chairman and Chief Executive Officer of Box USA Group, Inc., a corrugated box manufacturer, from 2000 to 2004. Mr. Stone served as President and Chief Executive Officer of Smurfit-Stone Container Corporation from 1999 to 2000. Prior to 1999, Mr. Stone was Chairman, President and Chief Executive Officer of Stone Container Corporation, a multinational paper company primarily producing and selling pulp, paper and packaging products. Mr. Stone, 70, joined McDonald's Board in 1989 and is a member of the class of 2007. He also serves as a director of Autoliv Inc.

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### ***Proposal No. 2. Approval of the Appointment of an Independent Registered Public Accounting Firm to Serve as Independent Auditors for 2005***

The Audit Committee is responsible for the appointment of the independent auditors engaged by the Company. The Audit Committee has appointed Ernst & Young LLP as independent auditors for 2005. The Board is asking shareholders to approve this appointment of Ernst & Young LLP, an independent registered public accounting firm, as independent auditors for 2005. Ernst & Young LLP audited the Company's financial statements and internal controls over financial reporting for 2004. A representative of that firm will be present at the Annual Shareholders Meeting and will have an opportunity to make a statement and answer questions.

*See page 25 for additional information regarding the independent auditors including a description of the Audit Committee's Policy for the Pre-Approval of Audit and Permitted Non-Audit Services, and a Summary of Auditor Fees and Services.*

***The Board of Directors recommends that shareholders vote FOR the appointment of Ernst & Young LLP, an independent registered public accounting firm, to serve as independent auditors for 2005.***

### ***Proposal No. 3. Shareholder Proposal Relating to Genetic Engineering of Food and Seed***

The Camilla Madden Charitable Trust, the Congregation of the Sisters of St. Joseph of Springfield, Massachusetts, The Sinsinawa Dominicans and The Sisters of St. Francis of Philadelphia advised the Company that they intend to present the following shareholder proposal at the Annual Shareholders Meeting. The addresses and the share ownership of the proponents will be furnished to any shareholder upon oral or written request to the Company's Investor Relations Department at 1-630-623-7428 or McDonald's Plaza, Oak Brook, IL 60523.

***The Board recommends a vote AGAINST this proposal.***

### **The Board's Recommendation**

McDonald's is committed to serving safe, quality products in our more than 30,000 restaurants in 119 countries. We provide customers an array of menu choices derived from a variety of safe and wholesome agricultural products. McDonald's does not plant or raise crops for use in our products. Therefore, the Company does not genetically engineer the ingredients it purchases for any of its products. Rather, we purchase the ingredients for our products from the agricultural industry. Such purchases are usually made regionally in the country or area of the world where our restaurants are located, and agricultural practices vary worldwide.

Like other purchasers of food products, we rely on scientific and regulatory authorities, such as the Food and Drug Administration (FDA) and the Department of Agriculture (USDA) in the U.S., and other international agencies, such as the United Nations, Codex Alimentarius, and other scientific bodies, to review or approve the use of various food ingredients. McDonald's uses products and ingredients that have been approved for use by these agencies.

Since one of our highest priorities is the health and safety of our customers and meeting their needs, we continuously review and monitor the status of regulatory approvals, customer acceptance, consumer benefits and choice, environmental impact and the state of scientific research to guide us in making purchasing decisions. For example, we have avoided genetically engineered food in some markets, such as Europe, due to a lack of customer acceptance.

The issue of biotechnology in food is complex and reaches far beyond McDonald's. We believe that relevant government agencies with scientific expertise are the best decision makers in this area. Accordingly, because the Company is a purchaser not a grower or producer of agricultural products, we believe preparing a report regarding genetically engineered products will not be a meaningful endeavor, nor will it impact the safety and quality of the ingredients we purchase. Therefore, **the Board of Directors recommends a vote AGAINST this shareholder proposal.**

### Shareholder Proposal

RESOLVED: Shareholders request that an independent committee of the Board review Company policies and procedures for monitoring genetically engineered (GE) products and report (at reasonable cost and omitting proprietary information) to shareholders within six months of the annual meeting on the results of the review, including:

- (i) the scope of Company products that are genetically engineered;
- (ii) the environmental impacts of continued use of GE products sold or manufactured by the Company;
- (iii) contingency plans for removing GE seed and other GE products from the ecosystem should circumstances so require; and
- (iv) evidence of independent long-term safety testing demonstrating that GE crops, organisms, or products thereof are actually safe for humans, animals and the environment.

### Supporting Statement

Indicators that genetically engineered organisms MAY be harmful to humans, animals, or the environment include:

*The report Safety of Genetically Engineered Foods: Approaches to Assessing Unintended Health Effects*

*(National Academy of Sciences [NAS] 7/2004) states: ...there remain sizable gaps in our ability to identify compositional changes that result from genetic modification of organisms intended for food; to determine the biological relevance of such changes to human health; to devise appropriate scientific methods to predict and assess unintended adverse effects on human health. (p. 15)*

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*The study Gone to Seed, (Union of Concerned Scientists, 3/2004), found that genetically engineered DNA is contaminating U. S. traditional seeds (corn, soybean, canola), and that if left unchecked could disrupt agricultural trade, unfairly burden the organic foods industry, and allow hazardous materials into the food supply.*

The FDA does not require producers of GE food products to seek prior FDA approval of finished GE food products; producers of GE-products are merely encouraged to have voluntary safety consultations with the FDA. The testing protocol on foods derived from biotechnology adopted in 2003 by the Joint UN FAO/WHO Codex Alimentarius Commission is not required by the FDA to assess GE foods on the U.S. market.

No post-marketing surveillance is in effect to verify pre-market screening for unanticipated adverse health consequences from the consumption of GE food. (NAS 7/2004)

European Union rules require traceability of food and feed ingredients to their source materials, and labeling of food containing more than 0.9% GE ingredients.

Insurers in Germany, the UK and elsewhere are refusing liability coverage for genetically engineered crops, an example of heightened concern about the long-term safety of GE crops.

Weed resistance to the herbicide used widely by farmers who plant genetically engineered herbicide resistant crops, is increasing. (Agriculture Research Service 8/24/04)

In December 2002, StarLink corn, not approved for human consumption, was detected in a U.S. corn shipment to Japan. StarLink first contaminated U.S. corn supplies in September 2000, triggering a recall of 300 products.

An August-September 2004 survey of 1,194 grain elevators across the United States conducted by the American Corn Growers Foundation Farmer Choice-Customer First program found that nearly one-quarter (23.7%) reported that they require segregation of biotech corn from conventional corn varieties.

We believe such a report will disclose information material to the company's future.

***For the reasons stated on page 9 of this Proxy Statement, your Board of Directors recommends you vote AGAINST this shareholder proposal.***

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**Table of Contents****Stock Ownership****Stock Ownership Guidelines**

The Company imposes minimum stock ownership guidelines for Directors and officers.

Each Director is expected to acquire, within five years after becoming a Director, common stock or common stock equivalent units equal in value to at least five times the annual retainer or 10,000 shares (of which 1,000 shares should be acquired within the first year) and to maintain that level of investment throughout his or her term.

Each officer is expected to acquire the lesser of the minimum share ownership requirements or value of shares as a multiple of base salary listed below within five years of becoming an officer, and to hold those shares during his or her term of office:

<u>Level/band</u>	<u>Minimum share ownership requirements</u>	<u>Value of shares as a multiple of base salary</u>
Chief Executive Officer	240,000	5x
President and Chief Operating Officer	180,000	5x
President, North America and Europe/ Senior Executive Management	85,000	4x
Executive Management	50,000	4x
Senior Leadership	25,000	3x
Leadership	8,500	1.5x

We review compliance with these requirements annually. Failure to meet these requirements may result in a reduction in future long-term incentive grants and/or payment of future annual and/or long-term incentive payouts in the form of common stock.

**Stock Ownership of Management**

The following table shows the ownership of the common stock and common stock equivalent units for the named individuals and the group as of March 1, 2005. Directors and Executive Officers as a group owned (directly, indirectly and through benefit plans) less than 1.0% of the Company's common stock.

<u>Name</u>	<u>Common stock (a, b, c, d)</u>	<u>Stock equivalents (e)</u>	<u>Total</u>
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Hall Adams, Jr.	26,002	9,406	35,408
Ralph Alvarez	259,280	20,086	279,366
Charles H. Bell (f)			
Edward A. Brennan	10,836	11,692	22,528
James R. Cantalupo (f)			
Robert A. Eckert	13,334	5,644	18,978
Enrique Hernandez, Jr.	28,402	24,676	53,078
Jeanne P. Jackson	16,252	14,997	31,249
M. Lawrence Light	184,099	0	184,099
Walter E. Massey	18,002	8,851	26,853
Andrew J. McKenna	54,642	51,724	106,366
Cary D. McMillan	13,334	5,467	18,801
Matthew H. Paull	319,482	12,522	332,004
Michael J. Roberts	681,695	21,032	702,727
John W. Rogers, Jr.	38,434	5,417	43,851
James A. Skinner	1,127,837	33,673	1,161,510
Anne-Marie Slaughter	0	936	936
Roger W. Stone	37,668	61,714	99,382
Directors and Executive Officers as a group (the Group)(21 persons)	3,667,547	297,809	3,965,356

- (a) Beneficial ownership of shares that are owned by members of their immediate families directly or through trusts is disclaimed as follows: Directors McKenna, 640; and Rogers, 100; and the Group, 740.
- (b) Includes unallocated shares held in the Company's Profit Sharing and Savings Plan as follows: Messrs. Light, 533; and Paull, 2,024; Directors Roberts, 10,038; and Skinner, 15,141; and the Group, 48,115.
- (c) Includes shares that could be purchased by exercise of stock options on or within 60 days after March 1, 2005 under the Company's option plans as follows: Directors Adams, 22,002; Brennan, 8,336; Eckert 3,334; Hernandez, 20,002; Jackson, 14,002; Massey, 18,002; McKenna, 16,002; McMillan, 3,334; Roberts, 643,125; Rogers, 3,334; Skinner, 925,068; and Stone, 19,668; Messrs. Alvarez, 259,272; Light, 159,625; and Paull, 311,925; and the Group, 3,136,799.
- (d) Directors and Executive Officers as a group have sole voting and investment power over shares of common stock listed above except as follows: (i) shared voting and investment powers for shares held by Directors Eckert, 10,000; Hernandez, 8,400; Jackson, 2,250; Roberts, 878; Skinner, 2,168; and the Group, 60,506; and (ii) for the benefit of children, shares held by Director Roberts, 200; and the Group, 416.
- (e) Includes common stock equivalent units credited under the Company's Supplemental Profit Sharing and Savings Plan, and the Directors Stock Plan, which are payable in cash.
- (f) Messrs. Bell and Cantalupo died prior to March 1, 2005, the date as of which the table speaks.

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### **Executive Compensation**

*The following report of the Compensation Committee of the Board of Directors outlines the Company's compensation philosophy and programs, and describes the processes the Committee employs in its compensation determinations. Following this report is the Summary Compensation Table showing compensation history for each of the Company's Chief Executive Officers during 2004 (Messrs. Cantalupo, Bell and Skinner) and four other Executive Officers (together, the Named Officers). Stock option grant and exercise information and long-term cash incentive information for each of these officers along with a Stock Performance Graph also follow this report. A listing of the Company's Executive Officers may be found on page 27.*

### **Compensation Committee Report on Executive Compensation**

*Dear Fellow Shareholders:*

Our Committee is composed entirely of independent Directors. In consultation with senior management, we establish the Company's general compensation philosophy, and oversee the development and implementation of executive compensation programs. Each year, we review and approve the Company's goals and objectives relevant to the compensation of the Chief Executive Officer and evaluate his performance in light of those goals and objectives. Based on this evaluation, and after consulting with other independent members of the Board of Directors, our Committee approves individual elements of the Chief Executive Officer's total compensation package. In accordance with the Company's Corporate Governance Principles, which describe the manner in which our Board operates, our Committee also approves the compensation structure for the Company's officers annually based on recommendations from management, and reviews and approves the compensation packages of senior management. As required by our charter, our Committee also reviews the Company's incentive compensation and welfare benefit plans, as well as the Company's policies with respect to post-service arrangements and any perquisites provided to officers. Our Committee Chairperson regularly reports on Committee actions and recommendations at Board meetings. In addition, the Chief Executive Officer's performance and senior management compensation are frequently discussed at executive sessions of the Board of Directors, when only non-management Directors are present.

### **Global total compensation philosophy**

The objective of the Company's global total compensation program is to attract, motivate, reward and retain talented and engaged people who can deliver strong performance and help the Company to achieve our business objectives. Consistent with this performance-based objective, our total compensation program emphasizes accountability for results and supports important performance drivers.

### **Executive compensation**

We believe that executive compensation should be competitive with other large globally branded companies and alternative careers within the McDonald's System (*i.e.*, careers as a franchisee or supplier). Our determinations are guided in part by the increasingly competitive demand for talented executives who have the skills and expertise required to lead a large, dynamic global business. In this regard, an overall review of competitive market data is conducted annually.



We review information supplied by independent consultants to determine the competitiveness of McDonald's total compensation package for senior management with that of a group of comparator companies (Comparator Group). In addition to reviewing competitive data, we also consider certain qualitative factors which we believe contribute to building McDonald's global brand.

In consultation with an independent consultant, the Committee revised its customized comparator group in 2004. Although some companies within the new Comparator Group are included in the Dow Jones Industrial Average shown in the Stock Performance Graph on page 15 of this Proxy Statement, the Comparator Group is not made up exclusively of companies used in that index. Instead, the Comparator Group includes 25 branded consumer products firms, key McDonald's competitors and global companies within the service/retail industry that are most likely to compete with McDonald's for executive talent. In 2004, the total compensation targets for executives were established to approximate the 60th percentile of the compensation levels of the Comparator Group, if stated performance goals were achieved. For 2004, cash compensation (base salary and annual incentives) paid to the Named Officers in the Summary Compensation Table on page 16 were above the median of this peer group's range, while long-term incentives paid to such officers approximated the middle of the range. Long-term equity incentive awards were adjusted slightly upward in 2005 for a select group of senior management in order to achieve our competitive objective.

### **Recent executive compensation actions**

As reported in last year's Proxy Statement, management and the Committee began conducting an in-depth compensation analysis in 2003 to ensure that, in today's dynamic environment, our total compensation philosophy and mix continue to be properly aligned with the Company's business strategy and the interests of our shareholders. To assist in this analysis, the Committee retained an independent consultant. The analysis focused on developing a reward system that supports our global business strategy to ensure strong accountability for business results, and puts a greater focus on performance differentiation, in order to reward and retain top performers.

As a result of this analysis, the Committee approved global changes to the Company's annual bonus program (Target Incentive Plan) in 2004 in order to provide greater line of sight and accountability for both business and individual results around the world. In addition, the long-term

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incentive element for senior management was redesigned to include a new long-term, performance-based cash incentive program (Cash Performance Unit Plan) for the 2004-2006 performance cycle in order to align these leaders toward a common focus on the long-term success of McDonald's, with a corresponding one-third reduction in the Company's stock option award guidelines applicable to senior management in 2004.

The Company continues to implement this new compensation strategy, and in 2005, the Committee made further adjustments to the Company's mix of long-term incentive compensation in order to optimize the use of equity-based compensation while providing programs that motivate and reward employees as well as provide the incentive for performance. In this regard, stock option award guidelines applicable to employees were reduced or eliminated beginning in 2005. The potential stock option value attributable to this reduction was shifted into cash-based incentives or other equity-based awards, such as restricted stock units. Beginning in 2005, the value of long-term incentives awarded to Executive Officers will be comprised of stock options (1/3), performance-based restricted stock units (1/3) and cash incentives under the Cash Performance Unit Plan (1/3). These adjustments support the Company's commitment to reduce the annual equity award usage rate (known as the run rate) as a percent of outstanding shares.

With these actions, the Committee believes that the Company's executive compensation policies and programs are better aligned with shareholders' interests, the external regulatory environment and the Company's Plan to Win management's key business strategy designed to revitalize the Brand by consistently delivering on the drivers of exceptional customer experiences.

## **Annual cash compensation**

Annual cash compensation for senior management, as for all employees, consists of base salary and a variable, at-risk incentive under our Target Incentive Plan (TIP) that is directly tied to annual business results and individual performance.

Our Committee annually approves an executive's base salary, taking into consideration the executive's level of responsibility and individual performance as well as competitive pay practices. Factors used in gauging individual performance are: developing and executing corporate strategies; leading and developing people; initiating and managing change; effectively managing the many relationships within the McDonald's System; and contributing to programs that positively impact the Company's performance.

Each year, the Committee approves performance targets (excluding the effects of foreign currency translation on reported results) as well as minimum threshold financial performance levels. Each employee is assigned a target incentive at the beginning of the year (the greater the individual's responsibility, the higher the percentage of target incentive to salary). Target incentives may be adjusted to reflect mid-year promotions. TIP awards are stated as a specified percentage of base salary as of the end of the year. No portion of the award is payable if the threshold level of performance is not attained. The final incentive payment depends on the actual performance achieved in comparison to the targets; however, the Committee may make adjustments to exclude the effects of certain unusual items to ensure that incentives reflect the underlying operating results of the Company.

A global TIP was designed in 2004 to link rewards to achievement of the Company's business objectives as well as specific key initiatives identified to help us achieve our worldwide strategies. All major McDonald's markets participated in a common annual incentive framework, supporting a consistent strategy and focus. For 2004, target incentives for all employees, including Executive Officers, were adjusted by team and individual performance factors based in part on performance of the Company or the employee's respective business unit, as measured by operating income. Operating income performance was then adjusted by specific modifiers including changes in comparable guest counts, the achievement of general and administrative expense targets, nonfinancial factors designed to improve Quality, Service & Cleanliness (QSC), employee satisfaction, employer image and other nonfinancial initiatives designed to enhance our Brand.

The Company significantly exceeded the operating income target applicable to all Named Officers in 2004. Therefore, consistent with TIP, team performance factors applicable to the Named Officers for 2004 were well above target. Although the performance factors approved by the Committee excluded the impact of the impairment and other charges incurred during the fourth quarter of 2004, target incentives awarded to all officers, including the Named Officers, were reduced in part as a result of these charges reflecting management's accountability for the Company's overall business decisions and results. The Summary Compensation Table on page 16 of this Proxy Statement lists the awards paid to the Named Officers for 2004 performance.

### **Long-term incentives**

Long-term incentives consist of stock options, restricted stock units and cash awards under a long-term incentive plan. These awards serve to focus executive attention on the long-term performance of the business and comprise a significant portion of total compensation for senior management consistent with our increased emphasis on the pay-for-performance element of executive compensation.

#### *Options*

Options typically have a life of ten years, vest ratably over four years, and have an exercise price equal to the fair market value of our common stock on the grant date. Each year, the Committee establishes stock option guidelines based on level of responsibility. Individual awards to employees, including members of senior management, are made within these guidelines, dependent primarily upon sustained individual performance and on the potential for positively influencing future results.

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### *Restricted stock units*

Restricted stock unit awards are designed to increase retention of top performers and relate directly to the enhancement of long-term shareholder value. Restricted stock units typically cliff vest after three years and are subject to risk of forfeiture. During 2004, the Committee granted a total of 195,000 restricted stock units to a select group of executives. In connection with their respective elections to Chief Executive Officer, and President and Chief Operating Officer in November 2004, Messrs. Skinner and Roberts received 40,000 and 30,000 performance-based restricted stock units, respectively. The Committee also awarded 25,000 performance-based restricted stock units at that time to Mr. Paull, reflecting his strong leadership in the area of financial discipline throughout the year. The vesting of these performance-based restricted stock units is contingent upon the Company's achievement of a target level of diluted earnings per share growth during a specified three-year cliff vesting period. The Summary Compensation Table on page 16 of this Proxy Statement describes awards of restricted stock units and options granted to the Named Officers in 2004.

### *Long-term incentive plan*

As a result of the total compensation analysis discussed earlier in this Report, a new Cash Performance Unit Plan (CPUP) was introduced for the performance period 2004-2006 for senior management. CPUP is a three-year, long-term incentive plan tied directly to the Company's Plan to Win. During the three-year period, performance will be measured by consolidated three-year compounded annual constant currency operating income growth (weighted 75%) and average return on total assets (weighted 25%). A multiplier based on McDonald's cumulative total shareholder return versus the S&P 500 Index will also be applied to either increase or decrease the amount of the award. The table on page 20 of this Proxy Statement sets forth the amount the Named Officers will receive if minimum, target or maximum performance is achieved during this three-year cycle.

## **Other compensation**

Executives participate in other broad-based benefit programs, such as the Company's retirement, life insurance and healthcare programs. In 2005, changes in the Company's Profit Sharing and Savings Plan were designed to encourage employees to increase their retirement savings while changes to our healthcare programs provide more focus on employee health and wellness. Under a new stratified premium structure, officers will pay higher premium rates than non-officer employees for health insurance coverage beginning in 2005.

Perquisites provided to executives generally include Company-provided cars, financial planning, annual physical examinations and limited personal use of the Company's aircraft. Additional information regarding perquisites provided to the Named Officers is set forth in the Summary Compensation Table on page 16 of this Proxy Statement.

## **Stock ownership requirements**

We believe that the Company's executives will more effectively pursue the interests of our shareholders, whose interests they are charged with enhancing, if they are shareholders themselves. Consistent with this philosophy, minimum share ownership requirements apply to all officers. All Executive Officers, including Mr. Skinner, are either in compliance with or are on target to achieve compliance within the required time frame. The Company's stock ownership requirements can be found on page 11 of this Proxy Statement.

## Compensation of the Chief Executive Officers

From a financial perspective, 2004 was an outstanding year for McDonald's. Top management demonstrated tremendous leadership in executing our key business strategy, the Plan to Win. This renewed focus on operational excellence, leadership marketing and innovation resulted in record sales and profits for the year. From a personal perspective, however, McDonald's experienced deep losses in 2004 with Jim Cantalupo's sudden death in April and Charlie Bell's decision to step down later in the year in order to focus on his battle with cancer. In November, the Board of Directors elected Jim Skinner as Chief Executive Officer to continue the Company's strategic focus established by Jim Cantalupo and Charlie Bell.

During 2004, each of these Chief Executive Officers participated in the compensation programs described throughout this Report. Amounts paid and awards granted to these officers are disclosed in the compensation tables beginning on page 16 of this Proxy Statement.

Mr. Cantalupo served as Chairman and Chief Executive until his death on April 19, 2004. Throughout his service to the Company, Mr. Cantalupo demonstrated focused leadership in developing and executing the Company's strategic initiatives, which helped produce extraordinary business results. The Company recognized Mr. Cantalupo's outstanding service to the Company by awarding a discretionary bonus to his estate in an amount similar to the bonus he would have received under TIP had he remained employed throughout the year. His estate also received a prorated payout under CPUP based upon Company performance prior to the date of his death.

Mr. Cantalupo's successor, Charlie Bell, served as President and Chief Executive Officer of the Company from April 19, 2004 until November 22, 2004, at which time he stepped down from that office due to health reasons. Following his death in January 2005, the Committee awarded an annual incentive award to Mr. Bell's estate of \$3,185,000 under TIP reflecting his strong leadership, his success in taking on the role of Chief Executive Officer under exceptional circumstances and the Company's remarkable financial results in 2004.

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As more fully described in the compensation tables beginning on page 16 of this Proxy Statement, all of Messrs. Cantalupo's and Bell's restricted stock units and stock options vested immediately upon death in accordance with their terms. In addition, their respective unexercised stock options will remain exercisable for up to five years after death.

The Board of Directors elected James Skinner as Chief Executive Officer on November 22, 2004. In recognition of his increased responsibilities, our Committee granted Mr. Skinner 250,000 stock options and 40,000 performance-based restricted stock units at the time of his promotion. As a result of this award, Mr. Skinner did not participate in the Company's broad-based equity grant in the first quarter of 2005. The Committee awarded an annual incentive award of \$2,198,000 to Mr. Skinner under TIP in recognition of his seasoned leadership throughout this remarkable year and his unrelenting focus on the Plan to Win, a program in which he has been integrally involved since its inception in early 2003.

### **Policy with respect to the \$1 million deduction limit**

Section 162(m) of the Internal Revenue Code of 1986 generally limits to \$1 million the tax deductibility of annual compensation paid to certain officers. However, performance-based compensation can be excluded from the limit so long as it meets certain requirements. While the Committee retains the flexibility to compensate executive performance that increases shareholder value, the Committee took steps in 2004 to maximize the Company's ability to deduct compensation expenses. The Committee believes that TIP, CPUP, stock options and the performance-based restricted stock units granted to the Executive Officers in 2004, as discussed above, satisfy the requirements for exemption under Section 162(m). Therefore, we expect substantially all 2004 compensation will qualify as a tax-deductible expense.

Submitted by the

### **Compensation Committee**

Edward A. Brennan, *Chairperson*

Hall Adams, Jr.

Robert A. Eckert

Jeanne P. Jackson

John W. Rogers, Jr.

Anne-Marie Slaughter

### **Stock Performance Graph**

The following performance graph compares the performance of the Company's common stock to the Standard & Poor's 500 Stock Index (S&P 500 Index) and to the performance of the companies comprising the Dow Jones Industrial Average (DJIA companies). The graph assumes that

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the value of the investment in the Company's common stock, the S&P 500 Index and the DJIA companies was \$100 at December 31, 1999 and that all dividends were reinvested.

At least annually, we consider which companies comprise a readily identifiable investment peer group. McDonald's is included in published restaurant indices; however, unlike most other companies included in these indices, which have no or limited international operations, McDonald's does business in 119 countries. For added perspective, a substantial portion of our operating income is generated outside the U.S. In addition, by virtue of our size, McDonald's inclusion in those indices tends to skew the results. Hence, we believe that such a comparison would not be meaningful.

On the other hand, our market capitalization, trading volume and importance in an industry that is vital to the U.S. economy have resulted in McDonald's inclusion in the Dow Jones Industrial Average since 1985. Thus, in the absence of any readily identifiable peer group for McDonald's, we believe that use of the DJIA companies as the group for comparison is appropriate. Like McDonald's, many DJIA companies generate meaningful sales and revenues outside the U.S., and some manage global brands.

The performance graph that follows shows McDonald's cumulative total shareholder returns (i.e., price appreciation and reinvestment of dividends) relative to the S&P 500 Index and the DJIA companies (including McDonald's) for the five-year period ended December 31, 2004. For the DJIA companies, returns are weighted for market capitalization as of the beginning of each period indicated. These returns may vary from those of the Dow Jones Industrial Average Index, which is not weighted by market capitalization and may be composed of different companies during the period under consideration.

McDonald's Corporation 15

**Table of Contents****Summary Compensation Table**

The following table summarizes the total compensation earned by or paid for services rendered in all capacities to the Chief Executive Officers and four other Executive Officers who were most highly compensated in 2004 (Named Officers). Executive Officers are designated by the Board of Directors.

Name and principal position	Year	Annual compensation		Long-term compensation			All other compensation
		Salary(\$)	Bonus(\$)	Awards		Payouts	
				Restricted stock	Securities underlying		
		Other annual compensation(\$)(a)	awards(\$)(b)			options(#)	
James A. Skinner	2004	\$ 900,344	\$ 2,198,000	\$ 1,248,400	375,000	0	\$ 188,221
Vice Chairman and Chief Executive Officer	2003	830,189	810,000	880,609	160,000	0	148,840
	2002	794,443	475,000	0	235,000	0	123,381
Michael J. Roberts	2004	671,937	1,600,000	1,770,000	300,000	0	146,028
President and Chief Operating Officer	2003	570,755	655,000	605,427	108,000	0	98,402
	2002	550,000	315,030	0	125,000	0	80,834
Matthew H. Paull	2004	578,120	1,015,000	780,250	75,000	0	112,263
Corporate Senior Executive Vice President and Chief Financial Officer	2003	508,138	442,000	550,391	120,000	0	81,142
	2002	400,000	220,620	0	85,000	0	56,670
M. Lawrence Light (d) Corporate Executive Vice President Global Chief Marketing Officer	2004	610,392	840,000	0	57,000	0	105,400
Ralph Alvarez	2003	581,877	347,376	0	80,000	0	11,038
	2002	187,718	283,000	500,000	225,000	0	0
President McDonald's North America	2004	464,847	920,000	555,800	72,000	0	101,173
James R. Cantalupo	2003(e)						
	2002(e)						
Former Chairman of the Board and Chief Executive Officer	2004	438,932	0	1,331,500	200,000	\$ 791,200(g)	2,262,749
	2003	1,400,000	2,125,000	2,289,600	400,000	0	172,200
	2002(f)						



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Charles H. Bell	2004	1,014,800	3,185,000	\$ 221,110	0	350,000	0(g)	227,228
	2003	837,736	1,050,000		1,431,000	200,000	0	131,653
Former President and Chief Executive Officer	2002	550,000	368,676		0	425,000	0	52,319

\* Long-Term Incentive Plan

- (a) The Company offers the following perquisites to its executives: (i) personal use of Company-provided cars, (ii) personal financial counseling, (iii) limited personal use of the corporate aircraft, which, beginning in 2005, is further limited to the Chief Executive Officer only and (iv) annual physical examinations. Executives are required to reimburse the Company for their personal use of Company-provided cars and the corporate aircraft in accordance with Company policies. In addition, in 2004, the Company provided a medically outfitted aircraft for transportation to Australia to Mr. Bell, as well as a gross-up payment of income taxes he incurred in connection with this flight. Each perquisite is valued based on the perquisite's incremental cost to the Company. Except as noted for Mr. Bell, the total value received by each executive was less than \$50,000 during each year reflected in the table. The amount reported for 2004 for Mr. Bell includes \$186,177 for the medically outfitted aircraft.

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- (b) The amounts represent the market value (based on the closing market price of the Company's common stock on the date of award) of restricted stock units (RSUs) awarded. In 2004, the total number of RSUs granted to the Named Officers is as follows: Messrs. Skinner, 40,000; Roberts, 60,000; Paull, 25,000; Light, 0; Alvarez, 20,000; Cantalupo, 50,000; and Bell, 0. Generally, RSUs vest at the end of three years from date of award, except the awards to Messrs. Cantalupo and Bell vested upon death. Certain of the RSUs awarded in 2004 to the Named Officers contain performance restrictions on vesting based upon the Company's achievement of target levels of diluted earnings per share growth during the vesting period as follows: Messrs. Skinner, 40,000; Roberts, 30,000; and Paull, 25,000. The number of unvested RSUs, and in the case of Mr. Light, restricted shares of common stock, held by each of the Named Officers as of December 31, 2004, is as follows: Messrs. Skinner, 101,538; Roberts, 102,308; Paull, 63,462; Light, 22,483; and Alvarez, 50,769. As of December 31, 2004, the value of the unvested RSUs and restricted shares held by each of the Named Officers is as follows: Messrs. Skinner, \$3,255,308; Roberts, \$3,279,994; Paull, \$2,034,592; Light, \$720,805; and Alvarez, \$1,627,654. At the discretion of the Company, the RSUs will be settled at or after the time they vest by the delivery of shares of common stock or the cash equivalent value. During the vesting period, dividends are neither payable nor accrued on the RSUs or restricted shares held by the Named Officers.
- (c) For 2004, these amounts represent matching contributions and allocations by the Company to: (i) the Profit Sharing and Savings Plan and (ii) the Supplemental Profit Sharing and Savings Plan as follows: Messrs. Skinner, \$22,560 and \$165,661; Roberts, \$17,827 and \$128,201; Paull, \$17,827 and \$94,436; Light, \$22,560 and \$82,840; Alvarez, \$17,827 and \$83,346; Cantalupo, \$22,560 and \$440,189; and Bell, \$18,693 and \$208,535. Amounts which have been included with respect to the Supplemental Profit Sharing and Savings Plan represent the Company's obligation to pay such amounts to participants. For 2003 and 2002, the amounts in the table also include premiums on group term life insurance and officer life insurance. In addition, the amount reported in 2004 for Mr. Cantalupo includes a discretionary bonus of \$1,800,000 paid to his estate following his death, as described in the Compensation Committee Report beginning on page 12 of this Proxy Statement.
- (d) Mr. Light joined the Company on September 3, 2002 as an Executive Officer. The amount reflected in the 2002 Bonus column includes both a sign-on bonus and a prorated bonus under the Company's annual bonus plan.
- (e) Since Mr. Alvarez was not an Executive Officer during 2002 and 2003, no information is given for those years.
- (f) Mr. Cantalupo was not an Executive Officer in 2002 when he began his transition employment under the Executive Retention Plan (Retention Plan). See page 22 for a description of the Retention Plan and the benefits Mr. Cantalupo received during 2002 under that plan. A stock option grant of 600,000 shares was awarded to Mr. Cantalupo in December 2002 after he agreed to become Chairman and Chief Executive Officer.
- (g) The Compensation Committee waived the achievement of the Company's three-year performance goals under its long-term incentive plan in order to provide an early pro rata payout to Mr. Cantalupo's estate following his death. This pro rata payout was based upon first-quarter 2004 performance results. To avoid adverse tax consequences to the Company, Mr. Bell's payout was not accelerated, and instead his estate will receive a prorated payout at the end of the performance cycle if the stated performance goals are achieved.

**Table of Contents****Stock Options**

Options have an exercise price equal to the fair market value of a share of common stock on the grant date, generally have a 10-year life, and vest in equal installments over periods of four years. Generally, options expire 30 days after termination of employment, however, the Company's equity compensation plans provide for accelerated vesting and an extended exercise period upon death, change of control, disability, retirement, and under other limited circumstances, upon termination of employment. The Compensation Committee has general authority to accelerate, extend or otherwise modify benefits under stock option grants. Subject to the approval of the Compensation Committee, options may be transferred to certain permissible transferees, including immediate family members, for no consideration.

The following table shows the value of the 2004 stock option grants to the Named Officers, determined as of the grant date using the Black-Scholes option-pricing model:

*Stock Option Grants in 2004*

Name	Individual grants				
	Number of securities underlying options granted(#)(a)	Percent of total options granted to employees in 2004	Exercise price \$/Sh	Expiration Date(b)	Grant date present value(c)
James A. Skinner	62,500	0.31%	\$ 26.63	2/16/14	\$ 525,000
	62,500	0.31	25.31	5/20/14	525,000
	250,000(d)	1.25	31.21	12/1/14	2,460,000
Michael J. Roberts	62,500	0.31	26.63	2/16/14	525,000
	62,500	0.31	25.31	5/20/14	525,000
	175,000(d)	0.87	31.21	12/1/14	1,722,000
Matthew H. Paull	37,500	0.19	26.63	2/16/14	315,000
	37,500	0.19	25.31	5/20/14	315,000
M. Lawrence Light	28,500	0.14	26.63	2/16/14	239,400
	28,500	0.14	25.31	5/20/14	239,400
Ralph Alvarez	36,000	0.18	26.63	2/16/14	302,400
	36,000	0.18	25.31	5/20/14	302,400
James R. Cantalupo	200,000	1.00	26.63	2/16/14	1,680,000
Charles H. Bell	150,000	0.75	26.63	2/16/14	1,260,000
	200,000	1.00	25.31	5/20/14	1,680,000

(a) In lieu of a single grant in 2004, eligible employees, including the Named Officers, received two equal-sized option grants on February 16, 2004 and May 20, 2004. However, Mr. Bell's latter grant was larger as a result of his promotion to Chief Executive Officer on April 19, 2004.

(b)

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The information contained in the table represents the expiration date for each grant at the time of grant. Pursuant to the terms of our equity compensation plan, option recipients may receive accelerated vesting and/or an adjusted exercise period upon termination of employment. Messrs. Cantalupo and Bell's options reflected in this table vested upon death and remain exercisable until April 19, 2007 and January 17, 2008, respectively.

- (c) The Black-Scholes model was used assuming a dividend yield of 1.50% for the February 16, 2004 and May 20, 2004 grants and 1.72% for the December 1, 2004 grant; a risk-free interest rate of 3.54% for the February 16, 2004 grant, 4.33% for the May 20, 2004 grant, and 4.08% for the December 1, 2004 grant; an expected stock price volatility based on historical experience of 28.7% for the February 16, 2004 grant, 28.5% for the May 20, 2004 grant, and 28.3% for the December 1, 2004 grant; and an expected option life based on historical experience of seven years. The attribution of values with the Black-Scholes model to stock option grants requires the input of subjective assumptions, as described above, including the expected volatility of a stock price. While the assumptions are believed to be reasonable, the reader is cautioned not to infer a forecast of earnings or dividends either from the model's use or from the values adopted for the model's assumptions. Any future values realized would ultimately depend upon the excess of the stock price over the exercise price on the date the option is exercised.
- (d) Messrs. Skinner and Roberts each received an additional stock option grant on December 1, 2004 in connection with their respective elections to Chief Executive Officer, and President and Chief Operating Officer.

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**Table of Contents***Aggregated Option Exercises in 2004 and Fiscal Year-End Option Values*

Name	Shares acquired on exercise	Value realized	Number of securities underlying unexercised options at 12/31/04(#)(b,c)	Value of unexercised in-the-money options at 12/31/04\$(d)
	(#)	\$(a)	Exercisable/unexercisable	Exercisable/unexercisable
James A. Skinner	60,000	\$ 623,250	748,193/675,000	\$ 3,415,120/3,736,550
Michael J. Roberts	58,000	689,812	526,250/486,500	2,184,415/2,747,215
Matthew H. Paull	88,000	795,386	232,300/226,500	1,195,692/2,272,084
M. Lawrence Light	0	0	132,500/229,500	1,459,750/2,516,880
Ralph Alvarez	15,000	175,662	195,147/184,375	1,010,374/1,612,796
James R. Cantalupo(e)	1,919,000	20,018,386	2,814,461/ 0	9,436,590/ 0
Charles H. Bell(f)	6,000	57,463	1,435,125/ 87,500	10,698,300/ 541,125

- (a) Calculated by subtracting the exercise price from the market value of the common stock on the exercise date, then multiplying by the number of shares exercised. All values are on a pretax basis.
- (b) The securities underlying the options are shares of common stock.
- (c) The option term was extended three years for substantially all employee optionees, including the Named Officers, for those options granted between May 1, 1999 and December 31, 2000 that have an exercise price greater than \$28.90.
- (d) Calculated using the market value of the common stock at December 31, 2004 (\$32.06 per share) less the option exercise price multiplied by the number of exercisable or unexercisable option shares, as the case may be. All values are on a pretax basis.
- (e) Prior to his death, Mr. Cantalupo exercised 176,000 options and realized \$1,740,904 in value. Upon Mr. Cantalupo's death, all of his options vested and were transferred to a beneficiary trust. Following his death, Mr. Cantalupo's beneficiary trust exercised 1,743,000 options in 2004 and realized \$18,277,482 in value. Fiscal year-end option values reflect securities held by his beneficiary trust on December 31, 2004.
- (f) In December 2004, the Compensation Committee accelerated the vesting of 655,000 options held by Mr. Bell and approved the transfer of 1,435,125 vested options to his spouse. Fiscal year-end option values reflect securities held by Mr. Bell and his spouse on December 31, 2004. As of that date, Mr. Bell held 87,500 unvested options with a value of \$541,125 and his spouse held 1,435,125 vested options with a value of \$10,698,300. All of Mr. Bell's unvested options vested on the date of his death, January 17, 2005.

**Table of Contents****Long-Term Incentives***Long-Term Incentive Plans Awards in 2004 (to be paid in March 2007)*

Name	Number of shares, units or other rights (#)	Performance or other period until maturation or payout (b)		Estimated future payouts under non-stock price-based plans(a)		
				Threshold (\$)	Target	
					(\$)	Maximum (\$)
James A. Skinner	2,480,556	1/1/04	12/31/06	\$ 0	\$ 2,480,556	\$ 5,705,279
Michael J. Roberts	1,694,444	1/1/04	12/31/06	0	1,694,444	3,897,221
Matthew H. Paull	818,333	1/1/04	12/31/06	0	818,333	1,882,166
M. Lawrence Light	735,000	1/1/04	12/31/06	0	735,000	1,690,500
Ralph Alvarez	870,000	1/1/04	12/31/06	0	870,000	2,001,000
James R. Cantalupo	3,600,000(c)		(c)	0	3,600,000	8,280,000
Charles H. Bell	2,888,889(d)		(d)	0	2,888,889	6,644,445

- (a) Award recipients have the right under the Company's Cash Performance Unit Plan to receive a cash payment based upon the achievement of performance goals. The amount reflected in the table represents the target cash payout each participant is eligible to receive under the program.
- (b) Awards are in the form of a cash incentive, based on achievement of performance goals set at the beginning of the performance cycle. Actual payouts are based on the achievement of these goals and a target incentive established by the Compensation Committee at the beginning of the performance cycle. Target incentives may be adjusted to reflect mid-cycle promotions. The information reported in the table reflects applicable mid-cycle promotions. No payout occurs unless the Company achieves certain threshold performance objectives. At the beginning of the 2004-2006 cycle, the Company established three-year financial performance goals for the Company that include compounded annual constant currency operating income growth (weighted 75%) and average return on total assets (weighted 25%). Payouts are also subject to a multiplier based on the Company's total shareholder return compared to that of the companies that make up the S&P 500 Index. A participant must be an employee at the end of the performance period to receive a payout. However, upon death or disability prior to the end of the performance period, payouts are prorated based on the portion of the performance period the individual was employed. Upon retirement prior to the end of the performance period, payouts are prorated based on the portion of the performance period the individual was employed and the Company's performance during the entire performance period.
- (c) The information contained in the table represents the award granted to Mr. Cantalupo in 2004. Under the terms of the plan, Mr. Cantalupo's estate received a prorated payout of \$791,200 following his death. See footnote (g) to the Summary Compensation Table on page 16.
- (d) The information contained in the table represents the award granted to Mr. Bell in 2004. Under the terms of the plan, as a result of Mr. Bell's death in January 2005, his estate is entitled to receive a prorated payout at the end of the performance cycle if the Company achieves its stated performance goals.

**Change of Control Employment Agreements**

The Company has entered into change of control employment agreements with some of its employees, including all of the Named Officers (however, the agreements with Messrs. Cantalupo and Bell are no longer effective). These agreements provide that, upon a change of control of the Company, the executives will be entitled to the benefits described below. An executive who also participates in the Executive Retention Plan must elect to receive severance benefits under either the Executive Retention Plan or these change of control agreements.

Subject to exceptions set out in the agreements, a change of control will occur if: a person or group acquires 20% or more of the Company's outstanding common stock or voting securities; the members of the Company's Board on the date of the agreements (and certain new Directors approved in a specified manner by those members) cease to constitute at least a majority of the Board as a result of an actual or threatened election contest; there is a merger or other business combination involving the Company, or a disposition of all or substantially all of the assets of the Company; or the shareholders of the Company approve a liquidation or dissolution of the Company.

#### **Benefits upon a change of control**

The agreements provide generally that, during the three-year period following a change of control, (i) the executive's position and authority may not be reduced, (ii) the executive's place of work may not be relocated by more than 30 miles, (iii) the executive's base salary may not be reduced, (iv) the executive's annual bonus opportunity may not be reduced and the annual bonus paid will not be less than the target annual bonus, and (v) the executive will continue to participate in employee benefit plans on terms not less favorable than before the change of control. In addition, within 30 days after a change of control, the Company will pay to each executive a prorated portion

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of that executive's annual bonus and of each outstanding LTIP award (both computed at the target levels) for the partial year or LTIP period prior to the change of control.

### **Termination for good reason**

The Company's failure to provide any of the benefits described above following a change of control will allow the executive to terminate his or her employment for good reason at any time during the three-year period following a change of control. The executive also may terminate his or her employment for good reason if, during the three-year period following a change of control: (i) there is a material adverse change in the executive's position or other terms of employment, (ii) the Company materially breaches the executive's agreement, (iii) the Company attempts to terminate the executive for cause without following requirements set forth in the executive's agreement, or (iv) a successor entity fails to assume the executive's agreement.

### **Severance benefits upon termination for good reason or without cause**

If the executive terminates his or her employment for good reason or is terminated by the Company without cause (as defined in the agreement) at any time during the three-year period following a change of control, then, in addition to the executive's entitlement to receive accrued but unpaid salary, bonus, deferred compensation and other benefit amounts due on termination, the executive will be entitled to the following severance benefits, subject to executing an agreement that includes a covenant not to compete, a covenant not to solicit employees, a nondisclosure covenant and a release of claims: a lump-sum cash payment equal to three times the sum of the executive's base salary, annual bonus (computed at the target level) and contribution received under the Company's defined contribution plan; a pro rata portion of the annual bonus (computed at the target level) for the year of termination; continued medical and life insurance benefits, as well as fringe and other benefits, for three years after the termination; and a lump-sum cash payment for any sabbatical leave that has been earned but not yet taken. In addition, for purposes of determining the executive's eligibility for any available post-retirement medical benefits, the executive will be treated as having three additional years of service and being three years older.

### **Severance benefits upon termination for other reasons**

In the case of the death or disability of an executive during the three-year period immediately following a change of control, the executive or his estate will be entitled to receive accrued but unpaid salary, bonus, deferred compensation and other benefit amounts due at the time of such death or disability at levels provided to his or her peer employees and at least as favorable as those in place immediately prior to the change of control.

If (i) the Company terminates an executive for cause following a change of control, (ii) an executive voluntarily terminates employment without good reason following a change of control or (iii) an executive who is otherwise eligible to receive severance benefits fails to execute the noncompetition and release agreement, then that executive will receive only a lump-sum payment of accrued but unpaid salary, bonus, deferred compensation and other benefit amounts due at the time of the termination.

### **Taxes**



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Subject to limitations specified in the agreements, the Company will reimburse an executive on an after-tax (grossed-up) basis for any parachute excise taxes incurred by that executive because of any payments or other amounts under the agreement or otherwise provided which are considered to be contingent upon a change of control.

### **Term of the agreements**

The agreements have an initial term of three years. However, one year after the date of the agreements, they are automatically extended in order to perpetually retain a two-year term until terminated by the Company with a minimum of two years' notice.

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### **Arrangements with Certain Executives**

#### **Executive Retention Plan**

The Company maintains an Executive Retention Plan (Retention Plan) under which select participants, including Messrs. Skinner, Roberts and Paull, will become entitled to certain benefits if they remain employed by the Company as an officer for a specified retention period. To receive these benefits, the participant must enter into and comply with an agreement that includes a covenant not to compete, a covenant not to solicit employees, a nondisparagement covenant, a nondisclosure covenant and a release of claims. The benefits are generally the same for all participants, but with specific differences as noted below.

Once a participant covered by the plan has completed his or her retention period, he or she may elect to enter the transition period, which continues for the lesser of 18 months or a number of months equal to the participant's total years of service. This election can only be made if a participant has reached the age of 62 or with the consent of the Chief Executive Officer (or the Compensation Committee, in the case of the Chief Executive Officer). During the transition period, the participant must agree to devote substantially all of his or her normal business time and efforts to the business of the Company in an officer position. During the transition period, the participant is entitled to receive: (i) base salary at the highest rate received by the participant before the transition period, (ii) a target-level annual incentive for any calendar year or years that end during the transition period and a prorated target-level incentive for any partial year at the end of the transition period, and (iii) prorated performance-based payouts for any partial LTIP cycles at the end of the retention period.

For a period of five years following the transition period, the participant must devote such time to the business of the Company as the Company may reasonably request. During this continued employment period, the participant is entitled to receive: (i) base salary at a rate equal to 35% of the base salary paid during the transition period (50% in the case of Mr. Skinner), and (ii) prorated performance-based payouts for any partial LTIP cycles at the end of the retention period. Participants will not receive annual or LTIP incentives during the continued employment period.

During both the transition period and the continued employment period, the participant will continue to participate in employee benefit plans, but will not be eligible to receive additional stock option grants, LTIP grants or other incentive compensation awards. Stock options and restricted stock units granted prior to the commencement of the transition period, however, will continue to vest and become exercisable in accordance with their original terms.

If a participant's employment is terminated by the Company during the retention period for any reason other than death, disability or cause (as defined in the plan), subject to the execution of an agreement as described above, the participant shall be entitled to payment of: (i) accrued but unpaid base salary and any annual incentive earned for prior years that has not been paid, (ii) an amount equal to the present value of salary and target-level incentives that would have been payable to the participant during his transition period and the present value of salary that would have been payable to the participant during the remainder of his continued employment period, and (iii) an amount equal to the estimated value of the participant's health and welfare benefits for the remainder of the transition and continued employment periods. Mr. Skinner would also receive five years of accelerated stock option vesting and exercisability for stock options, while Messrs. Paull and Roberts and all other participants would receive three years of accelerated stock option vesting and exercisability for stock options. In addition, Mr. Skinner has the right to terminate his employment for good reason (as defined in the plan) at any time during his retention and transition periods and receive the severance benefits described in this paragraph. During both the transition period and continued employment period, a participant's employment can only be terminated by the Company for cause or disability.

The plan is in effect until the later of October 24, 2007 or two years after the Company gives notice to all participants of its intention to terminate the plan. No additional employees will be added to this plan.

Mr. Skinner has completed his retention period. The retention period for Messrs. Paull and Roberts and all other participants ends on October 29, 2005.

Prior to January 1, 2003, Mr. Cantalupo was serving as a transition officer pursuant to the terms of the Retention Plan as in effect at that time, and received benefits thereunder, including an annual incentive award for 2002 and an LTIP payout for the performance cycle ended December 31, 2002 (both computed at target). Upon becoming Chief Executive Officer on January 1, 2003, Mr. Cantalupo ceased receiving benefits under the Retention Plan.

#### **Arrangement with M. Lawrence Light**

The Company has agreed to offer Mr. Light continued employment for a period of two and one-half years at a salary of \$50,000 per year when he ceases to be the Company's chief marketing officer. During this continued employment period, Mr. Light's equity incentives will continue to vest and be exercisable, and he may only be terminated for cause. For purposes of this arrangement, "cause" generally includes willful failure to perform assigned duties, violation of the Company's policies, and commission of acts involving fraud, breach of fiduciary duty or illegality. In order to remain employed on these terms, Mr. Light would have to enter into a non-competition agreement with the Company that would prevent him from providing services to a competing business for two years following his termination of employment.

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### **Certain Relationships and Related Transactions**

The McDonald's System has more than 30,000 restaurants worldwide, many of which are independently owned and operated. Within this extensive System, it is not unusual for our business to touch many companies in many industries, including suppliers of food and paper products. The Board reviews any relationship involving Board members in accordance with the Board's Standards on Director Independence, which is attached as Appendix B. Based on the Board's review of the pertinent facts and circumstances and taking into consideration all applicable laws, regulations and stock exchange listing requirements, the Board determined that the following relationships are not material and do not affect the independence of the Directors involved.

In 2004, the Company and its subsidiaries purchased approximately \$1.3 million worth of paper and other printed products (principally tray liners, french fry bags, hash brown bags and bag stuffers) from Schwarz Paper Company. Mr. McKenna is Chairman of Schwarz Paper Company, as well as a 59% shareholder of Schwarz. Members of Mr. McKenna's family are also shareholders of Schwarz. Schwarz's business with the Company and its subsidiaries represents less than 1% of Schwarz's total revenues. The Company believes that these purchases were made on terms at least as favorable as would have been available from other parties and intends to continue its dealings with Schwarz in 2005 on similar terms.

In 2004, the Company and its subsidiaries purchased approximately \$4.0 million worth of salad packaging and parfait cups from Prairie Packaging, Inc. Mr. Stone is a director of Prairie Packaging as well as a 6.39% shareholder. In addition, Mr. Stone's children are shareholders of Prairie Packaging. The Company believes that these purchases, which represent less than 1.5% of the revenues of Prairie Packaging, were made on terms at least as favorable as would have been available from other parties, and intends to continue its dealings with Prairie Packaging in 2005 on similar terms.

In 2004, as part of its ongoing share repurchase program, the Company purchased 15,009 shares of its common stock at the NYSE closing price on the date of purchase from Mr. Bell for \$456,274. Of the shares repurchased, 5,750 shares were acquired by Mr. Bell within two years prior to their sale through the exercise of stock options for \$80,242. The remaining 9,259 shares were acquired by Mr. Bell more than two years prior to their sale.

Following Mr. Bell's resignation as the Company's President and Chief Executive Officer, the Board authorized the Company to purchase Mr. Bell's Illinois residence. This purchase was completed substantially in accordance with the Company's relocation policy in December 2004 for a price of \$2,975,000. Under this policy, the Company obtained three independent, certified appraisals, disregarded the appraisal with the greatest difference from the middle-valued appraisal and averaged the remaining two appraisals.

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### **Audit Committee Matters**

#### **Audit Committee Report**

*Dear Fellow Shareholders:*

The Audit Committee is composed of four Directors, each of whom meets the independence and other requirements of the New York Stock Exchange. As stated previously, Enrique Hernandez, Jr., Cary D. McMillan and Roger W. Stone qualify as the audit committee financial experts. The Committee has the responsibilities set out in its charter, which has been adopted by the Board of Directors and is reviewed annually.

Management is primarily responsible for the Company's financial statements, including the Company's internal control over financial reporting. Ernst & Young LLP, the Company's independent auditors, is responsible for performing an audit of the Company's annual consolidated financial statements in accordance with generally accepted accounting principles (GAAP) and the Company's internal controls over financial reporting and for issuing reports on the statements and internal controls. Ernst & Young also reviews the Company's interim financial statements in accordance with Statement on Auditing Standards No.100 (interim financial information). The Committee oversees the Company's financial reporting process and internal control structure on behalf of the Board of Directors. The Committee met nine times during 2004, including meeting regularly with Ernst & Young and the internal auditors, both privately and with management present.

In fulfilling its oversight responsibilities, the Committee reviewed and discussed with management and Ernst & Young the audited and interim financial statements, including Management's Discussion and Analysis, included in the Company's Reports on Form 10-K and Form 10-Q. These reviews included a discussion of:

critical accounting policies of the Company;

the reasonableness of significant financial reporting judgments made in connection with the financial statements, including the quality (and not just the acceptability) of the Company's accounting principles;

the clarity and completeness of financial disclosures;

the effectiveness of the Company's internal control over financial reporting, including management's and Ernst & Young's reports thereon, the basis for the conclusions expressed in those reports and changes made to the Company's internal control over financial reporting during 2004;

items that could be accounted for using alternative treatments within GAAP, the ramifications thereof and the treatment preferred by Ernst & Young;

the annual management letter issued by Ernst & Young, management's response thereto and other material written communications between management and Ernst & Young;

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unadjusted audit differences noted by Ernst & Young during its audit of the Company's annual financial statements; and

the potential effects of regulatory and accounting initiatives on the Company's financial statements.

In connection with its review of the Company's annual consolidated financial statements, the Committee also discussed with Ernst & Young other matters required to be discussed with the auditors under Statement on Auditing Standards No. 61, as modified or supplemented (communication with audit committees) and those addressed by Ernst & Young's written disclosures and its letter provided under Independence Standards Board Standard No. 1, as modified or supplemented (independence discussions with audit committees).

The Committee is responsible for the engagement of the independent auditors and appointed Ernst & Young to serve in that capacity during 2004 and 2005. In that connection, the Committee:

reviewed Ernst & Young's independence from the Company and management, including Ernst & Young's written disclosures described above;

reviewed periodically the level of fees approved for payment to Ernst & Young and the pre-approved non-audit services it has provided to the Company to ensure their compatibility with Ernst & Young's independence; and

reviewed Ernst & Young's performance, qualifications and quality control procedures.

Among other matters, the Committee also:

reviewed the scope of and overall plans for the annual audit and the internal audit program;

consulted with management and Ernst & Young with respect to the Company's processes for risk assessment and risk management;

reviewed the adequacy of certain of the Company's financial policies;

reviewed and approved the Company's policies for the pre-approval of audit and permitted non-audit services by the independent auditors and the hiring of former employees of the independent auditors;

in 2003, established a policy for the submission and confidential treatment of communications received from employees and third parties about accounting, internal controls and auditing matters, and reviewed reports of such communications in accordance with the policy;

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reviewed with management the scope and effectiveness of the Company's disclosure controls and procedures, including for purposes of evaluating the accuracy and fair presentation of the Company's financial statements in connection with certifications made by the Chief Executive Officer and Chief Financial Officer; and

reviewed significant legal developments and the Company's processes for monitoring compliance with law and Company policies.

Based on the reviews and discussions referred to above, the Committee recommended to the Board of Directors the audited financial statements be included in the Company's Annual Report on Form 10-K for the year ended December 31, 2004 for filing with the SEC.

Respectfully submitted,

**The Audit Committee**

Enrique Hernandez, Jr., *Chairperson*

Walter E. Massey

Cary D. McMillan

Roger W. Stone

**Policy for Pre-Approval of Audit and Permitted Non-Audit Services**

The Audit Committee has implemented a policy for the pre-approval of all audit and permitted non-audit services proposed to be provided to the Company by its independent auditors. Under the policy, the Audit Committee may pre-approve engagements on a case-by-case basis or on a class basis if the relevant services are predictable and recurring.

Pre-approvals for classes of services are granted at the start of each fiscal year. In considering pre-approvals on a class basis, the Audit Committee reviews a description of the scope of services falling within each class and imposes specific budgetary guidelines that are largely based on historical costs. Pre-approvals granted on a class basis are effective for the applicable fiscal year.

Any audit or permitted non-audit service that is not included in an approved class, or for which total fees are expected to exceed the relevant budgetary guideline, must be pre-approved on an individual basis. Pre-approval of any individual engagement may be granted not more than one year before commencement of the relevant service. Pre-approvals of services that may be provided over a period of years must be reconsidered each year in light of all the facts and circumstances, including compliance with the pre-approval policy and the compatibility of the services with the auditor's independence.

The Corporate Controller monitors services provided by the independent auditors and overall compliance with the pre-approval policy. The Corporate Controller reports periodically to the Audit Committee about the status of outstanding engagements, including actual services

provided and associated fees, and must promptly report any noncompliance with the pre-approval policy to the Chairperson of the Audit Committee.

The complete policy is available on the Company's website at [www.governance.mcdonalds.com](http://www.governance.mcdonalds.com).

### Auditor Fees and Services

The following table presents fees billed for professional services rendered for the audit of the Company's annual financial statements for 2004 and 2003 and fees billed for other services provided by our independent auditors in each of the last two years:

<u>In millions</u>	<u>2004</u>	<u>2003</u>
Audit fees (a)	\$ 8.7	\$ 6.3
Audit-related fees (b)	.2	.3
Tax fees (c)	2.3	2.3
Other fees (d)	.1	.1
	<u>\$ 11.3</u>	<u>\$ 9.0</u>

- (a) Fees for services associated with the annual audit (including internal control reporting under Section 404 of the Sarbanes-Oxley Act), statutory audits required internationally, reviews of the Company's quarterly reports on Form 10-Q, and accounting consultations. The significant increase in audit fees in 2004 was driven by additional fees related to the Section 404 internal control reporting (\$1.6 million) and the weaker U.S. Dollar.
- (b) Fees for employee benefit plan audits, certain attestation services not required by statute or regulation and documentation assistance related to internal control reporting under Section 404 of the Sarbanes-Oxley Act.
- (c) Primarily fees for tax compliance in various international markets including expatriate tax services.
- (d) Fees for miscellaneous advisory services.



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### **Solicitation of Proxies and Voting**

### **Record Date and Voting at the Annual Shareholders Meeting**

Shareholders owning McDonald's common stock at the close of business on March 14, 2005 (the record date), may vote at the 2005 Annual Shareholders Meeting. On that date, 1,267,119,628 shares of common stock were outstanding. Each share is entitled to one vote on each matter to be voted upon at the Annual Shareholders Meeting.

Most shareholders have a choice of voting over the internet, by telephone or by using a traditional proxy card. Refer to your proxy or voting instruction card to see which options are available to you and how to use them.

The internet and telephone voting procedures are designed to authenticate shareholders' identities and to confirm that their instructions have been properly recorded.

If you properly sign and return your proxy card or complete your proxy via the telephone or the internet, your shares will be voted as you direct. If you sign and return your proxy but do not specify how you want your shares voted, they will be voted FOR the election of all nominees for Director as set forth under Election of Directors, FOR the approval of the independent auditors and AGAINST the shareholder proposal. You may revoke your proxy and change your vote at any time before the Annual Shareholders Meeting by submitting written notice to the Secretary, by submitting a later dated and properly executed proxy (including by means of a telephone or internet vote) or by voting in person at the Annual Shareholders Meeting.

All votes cast at this year's Annual Shareholders Meeting will be tabulated by Computershare Investor Services, LLC (Computershare), which has been appointed independent inspector of election. Computershare will determine whether or not a quorum is present.

With respect to the election of Directors, shareholders may vote (a) in favor of each of the nominees, or (b) to withhold votes as to specific nominees. Directors are elected by a plurality vote so the five nominees named on page 7 of this Proxy Statement receiving the greatest number of votes will be elected. Computershare will treat votes withheld as shares present for purposes of determining a quorum. Withheld votes will not affect the outcome of the election.

With respect to the approval of the independent auditors and the shareholder proposal, shareholders may vote (a) in favor of the matter, (b) against the matter, or (c) abstain from voting on the matter. Computershare will treat abstentions as shares present for purposes of determining a quorum. Since a majority of the shares represented at the meeting and entitled to vote is required for approval of these matters, abstentions will have the effect of a vote against approval.

Under NYSE rules, the proposals to elect Directors and to approve the appointment of independent auditors are considered discretionary items. This means that brokerage firms may vote in their discretion on these matters on behalf of clients who have not furnished voting instructions at least 15 days before the date of the Annual Shareholders Meeting.

In contrast, the proposal to approve the shareholder proposal is a non-discretionary item. This means brokerage firms that have not received voting instructions from their clients on this matter may not vote on this proposal. These so-called broker non-votes will not be considered in determining the number of votes necessary for approval and, therefore, will have no effect on the outcome of the vote for this proposal.

### **Proxy Solicitation**

The 2005 Proxy Statement and proxy card were mailed to shareholders beginning on or about April 6, 2005 in connection with the solicitation of proxies by the Board of Directors to be used at the 2005 Annual Shareholders Meeting. The cost of soliciting proxies will be paid by the Company. The Company has retained Innisfree M&A Incorporated to aid in the solicitation at a fee of \$15,000 plus reasonable out-of-pocket expenses. Proxies also may be solicited by employees and Directors of the Company by mail, by telephone, by facsimile, by e-mail or in person.

### **Confidential Voting**

It is the Company's policy to protect the confidentiality of shareholder votes. Throughout the voting process, your vote will not be disclosed to the Company, its Directors, officers or employees, except to meet legal requirements or to assert or defend claims for or against the Company or except in those limited circumstances where (1) a proxy solicitation is contested; or (2) you authorize disclosure. The inspector of election has been and will remain independent of the Company.

Nothing in this policy prohibits you from disclosing the nature of your vote to the Company, its Directors, officers or employees, or impairs voluntary communication between you and the Company, nor does this policy prevent the Company from ascertaining which shareholders have voted or from making efforts to encourage shareholders to vote.

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**Additional Information**

**Code of Ethics for the Chief Executive Officer and Senior Financial Officers**

*The Code of Ethics for the Chief Executive Officer and Senior Financial Officers is attached as Appendix G.*

**Executive Officers**

As stated in the Corporate Governance Principles, the Chief Executive Officer selects other Executive Officers with the approval of the Board of Directors. The following list sets forth the names of our Executive Officers, their ages and their positions.

**Ralph Alvarez**

Age: 49. President McDonald's North America

**M. Lawrence Light**

Age: 63. Corporate Executive Vice President Global Chief Marketing Officer

**Matthew H. Paull**

Age: 53. Corporate Senior Executive Vice President and Chief Financial Officer

**David M. Pojman**

Age: 45. Corporate Senior Vice President Controller

**Michael J. Roberts**

Age: 54. President and Chief Operating Officer

**Gloria Santona**

Age: 54. Corporate Executive Vice President, General Counsel and Secretary

**James A. Skinner**

Age: 60. Vice Chairman and Chief Executive Officer

**Russell P. Smyth**

Age: 48. President McDonald's Europe

**McDonald's Corporation Annual Report on Form 10-K, Other Reports and Policies**

Shareholders may access financial and other information on the investor section of the Company's website at [www.investor.mcdonalds.com](http://www.investor.mcdonalds.com). Also available, free of charge, are copies of the Company's 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 Securities Exchange Act of 1934 as soon as reasonably practicable after filing such material electronically or otherwise furnishing it to the SEC. Copies of financial and other information are available free of charge by calling 630-623-7428 or by sending a request to McDonald's Corporation, Investor Relations Service Center, Department 300, McDonald's Plaza, Oak Brook, IL 60523.

Also posted on McDonald's website are the Company's Corporate Governance Principles; the charters of McDonald's Audit Committee, Compensation Committee, Governance Committee, Corporate Responsibility Committee and Finance Committee; the Company's Standards of Business Conduct; the Code of Ethics for the Chief Executive Officer and Senior Financial Officers; the Code of Conduct for the Board of Directors; and the Policy for Pre-Approval of Audit and Permitted Non-Audit Services. Copies of these documents are also available free of charge by calling 630-623-7428 or by sending a request to McDonald's Corporation, Investor Relations Service Center, Department 300, McDonald's Plaza, Oak Brook, IL 60523.

**Householding of Annual Meeting Materials**

We are sending only one copy of the Company's Summary Annual Report, Financial Report and Notice of Annual Meeting and Proxy Statement to shareholders who share the same last name and address unless they have notified us that they wish to continue receiving multiple copies. This

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method of delivery, known as householding, will help ensure that shareholder households do not receive multiple copies of the same document and will help reduce our printing and postage costs, as well as save natural resources.

If you are a MCDirect Shares participant, hold McDonald's stock certificates or have book-entry shares in safekeeping at Computershare, you can opt out by calling 1-800-621-7825 (toll-free) from the U.S. and Canada, or 1-312-360-5129 (collect) from other countries, or write to Computershare Investor Services, Attn.: McDonald's Shareholder Services, 2 North LaSalle Street, Chicago, IL 60602. If you would like to opt out of this practice and your shares are held in street name, please contact your broker or bank.

If you are receiving multiple copies of the Summary Annual Report, Financial Report and/or Notice of Annual Meeting and Proxy Statement at your household and would prefer to receive a single copy of these materials, please contact Computershare Investor Services at the above numbers or address. If your shares are held in street name, contact your bank or broker.

If you would like additional copies of the Summary Annual Report, Financial Report and/or Notice of Annual Meeting and Proxy Statement, please go to [www.investor.mcdonalds.com](http://www.investor.mcdonalds.com) or call 630-623-7428.

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### **Appendix A. Corporate Governance Principles**

*The following is the complete text of McDonald's Corporate Governance Principles. Several of the policies and governance documents that are based on these Governance Principles are attached to this Proxy Statement. These policies and governance documents plus others are available on the Company's website at [www.governance.mcdonalds.com](http://www.governance.mcdonalds.com).*

McDonald's Corporation's Board of Directors is entrusted with, and responsible for, the oversight of the assets and business affairs of McDonald's Corporation in an honest, fair, diligent and ethical manner. This Board has long believed that good corporate governance is critical to our fulfilling our obligations to shareholders. We have tried to be a leader in this area, having adopted written governance principles as early as 1994. We were among the first to memorialize our governance principles, to regularly evaluate them and to publish information about them annually in our proxy statement. We firmly believe that good governance is a journey, not a destination. Therefore, we are committed to reviewing our governance principles at least annually, with a view to continuous improvement. As our governance processes evolve, we will change this document. One thing that we will not change, however, is our commitment to ensuring the integrity of the Company in all of its dealings with stakeholders. Our continued focus on leadership in corporate governance is an integral part of fulfilling our commitment to shareholders.

### **Roles and Responsibilities**

#### **Role of the Board**

The Board, which is elected by the shareholders, is the ultimate decision-making body of the Company, except with respect to matters reserved to shareholders. The primary function of the Board is oversight. The Board, in exercising its business judgment, acts as an advisor and counselor to senior management and defines and enforces standards of accountability—all with a view to enabling senior management to execute their responsibilities fully and in the interests of shareholders. The following are the Board's primary responsibilities:

Overseeing the conduct of the Company's business so that it is effectively managed in the long-term interest of shareholders;

Selecting, evaluating and compensating the Chief Executive Officer (CEO) and planning for CEO succession, as well as monitoring management's succession planning for other key executives;

Reviewing, approving and monitoring the Company's strategic plans and objectives;

Monitoring the Company's accounting and financial reporting practices and reviewing the Company's financial and other controls;

Overseeing the Company's compliance with applicable laws and regulations; and

Overseeing the processes that are in place to safeguard the Company's assets and mitigate risks.

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In performing its oversight function, the Board is entitled to rely on the advice, reports and opinions of management, counsel, auditors and outside experts. In that regard, the Board and its Committees shall be entitled, at the expense of the Company, to engage such independent legal, financial or other advisors as they deem appropriate, without consulting or obtaining the approval of any officer of the Company.

### **Role of the Chairman**

The Chairman shall be a member of the Board of Directors, and may, or may not, be, an officer or employee of the Company. A non-executive Chairman shall not be an officer or employee of the Company. The principal duty of the Company's Chairman is to lead and oversee the Board of Directors. The Chairman should facilitate an open flow of information between management and the Board, and should lead a critical evaluation of Company management, practices and adherence to the Company's strategic plan and objectives. In accordance with the Company's By-laws, the Chairman shall preside at all meetings of the Board and the shareholders. The Chairman, in consultation with the CEO, shall also establish an agenda for each meeting of the Board.

### **Role of the CEO and Management**

The Company's business is conducted by its employees, managers and officers, under the direction of senior management and led by the CEO. In carrying out the Company's business, the CEO and senior management are accountable to the Board and ultimately to shareholders. Management's primary responsibilities include the day-to-day operation of the Company's business, strategic planning, budgeting, financial reporting and risk management; and in fulfilling those responsibilities, management must balance the unique relationships between and among the McDonald's System of employees, franchisees, suppliers and customers.

### **Composition of the Board**

#### **Size of the Board**

The Board itself determines its size within the range of 11 to 24 members required by the Company's Certificate of Incorporation. The Board believes that, at this time, the desirable number of Directors is between 11 and 15.

### **Qualifications and Selection of Directors**

The Governance Committee is responsible for selecting candidates for Board membership, subject to Board approval, and for extending invitations to join the Board. In selecting candidates, the Board endeavors to find individuals of high integrity who have a solid record of accomplishment in their chosen fields and who display the independence of mind and strength of character to effectively represent the

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best interests of shareholders. Candidates are selected for their ability to exercise good judgment, and to provide practical insights and diverse perspectives. Consistent with its charter, the Governance Committee is responsible for screening candidates, for establishing criteria for nominees, and for recommending to the Board a slate of nominees for election to the Board at the Annual Meeting of Shareholders. Candidates are approved by the full Board.

## **Independence of Directors**

A substantial majority of Directors shall be independent of management. It is the intent of the Board that all newly appointed or elected non-management Directors shall be independent. An independent Director is one who is free of any relationship with the Company or its management that may impair, or appear to impair, the Director's ability to make independent judgments. The Board of Directors determines each Director's independence after reviewing pertinent facts and circumstances in accordance with these Principles and the independence standards established by the Board. If a change in circumstance affects an independent Director's continuing independence under the Board's independence standards, that Director shall offer to submit his or her resignation to the Chair of the Governance Committee. The Governance Committee shall determine whether to accept or reject such offer.

## **Management Directors**

The only management members of the Board shall be the CEO and the President. The CEO and the President shall resign from the Board at the time that his or her service in that capacity terminates.

## **Retirement; Term Limits**

A Director will be expected to retire on the date of the Annual Meeting of Shareholders immediately following his or her 73rd birthday, although the full Board may nominate existing members of the Board over the age of 73 as candidates in exceptional circumstances. The Board does not believe that arbitrary term limits on Directors' service are appropriate as they may sometimes force the Company to lose the contribution of Directors who have over time developed increased insight into the Company and its operations. However, a Director's service should not outlast his or her ability to contribute and consequently the Board does not believe that Directors should expect to be renominated continually until they reach the age of 73. Each Director's continued tenure shall be reconsidered at the end of his or her term, taking into account the results of the Board's most recent self-evaluation. It is the Board's intent to maintain a balance of Directors who have longer terms of service and those who have joined more recently.

## **Board Leadership**

### **Selection of CEO and Chairman**

The non-management Directors shall select the CEO and the Chairman. The non-management Directors will exercise their discretion in combining or separating the positions of Chairman and CEO, as they deem appropriate in light of prevailing circumstances.



### **Presiding Director**

The role of the Presiding Director is to preside at all executive sessions of the Board of Directors and to be an avenue for communications with non-management Directors. If the Company has a non-executive Chairman, then the Chairman shall be the Presiding Director. If the Chairman is a management Director, the Chair of the Governance Committee shall be the Presiding Director.

### **Responsibilities and Conduct of Directors**

#### **Responsibilities of Directors**

Directors must devote sufficient time and attention, and meet as frequently as necessary, to discharge their responsibilities. In discharging their responsibilities, Directors must exercise their business judgment and act in a manner that they believe in good faith is in the long-term best interests of the Company and its shareholders. Directors are expected to attend the Company's Annual Meeting of Shareholders, and all or substantially all Board meetings and meetings of the Committees of the Board on which they serve. Directors are also expected to spend whatever additional time as may be necessary for them to discharge their responsibilities appropriately. Directors shall ensure that other existing or future commitments do not materially interfere with their ability to fulfill their responsibilities as Company Directors.

#### **Other Board Service by Management Directors**

The CEO shall not serve on the boards of more than two listed companies, in addition to the McDonald's Board. The CEO shall obtain the approval of the Board before accepting an invitation to serve on the Board of another listed company.

#### **Other Board Service by Non-management Directors**

Whether service on the boards of directors of other companies is likely to interfere with the performance of a Director's duties to the Company depends on the individual and the nature of the Director's other activities. It is expected that, before accepting another board position, a Director will consider whether that service will compromise his or her ability to perform his or her present responsibilities to the Company. Each non-management Director shall provide advance notice to the Chairman and the Chair of the Governance Committee of acceptance of an invitation to serve on the Board of any other listed company. It is the Board's position that no Director shall serve on more than five boards of listed companies, in addition to his or her service on the McDonald's Board.

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### **Change of Circumstance**

If a Director's principal occupation or business association changes, or if other similarly material changes in a Director's circumstances occur, the Director shall offer to submit his or her resignation to the Chair of the Governance Committee. The Governance Committee shall determine whether to accept or reject such offer.

### **Code of Conduct for Directors**

Directors shall adhere to the *Code of Conduct for Directors*.

### **Conflicts of Interest**

Directors shall avoid any situation that may give rise to a conflict of interest or the appearance of a conflict of interest. If an actual or potential conflict of interest arises, the Director shall promptly inform the Chairman of the Board and the Chair of the Governance Committee (or in the event a potential conflict arises with the Chair of the Governance Committee, he or she shall notify the Chair of the Audit Committee) and recuse himself or herself from any Board deliberations or decisions related to the matter that is the subject of the conflict of interest. If an actual or potential conflict exists and cannot be resolved by a Director's recusal from participation in discussions or deliberations related to the matter or in any other reasonable manner, the Director shall offer to submit his or her resignation to the Chair of the Governance Committee. The Governance Committee shall determine whether to accept or reject such offer. The Board shall resolve any conflict of interest question involving the CEO or any executive officer.

### **Functioning of the Board**

#### **Board Meetings**

The Board of Directors meets at least six times a year. Additional meetings are scheduled as necessary or appropriate in light of prevailing circumstances. The Chairman chairs all meetings of the Board of Directors. The Chairman, in consultation with the CEO, establishes an agenda for each meeting. Agendas are set so as to ensure that the Board will be able to fulfill its oversight responsibilities. Directors may at any time suggest the addition of any matters to a meeting agenda or raise for discussion at any meeting any subject that they wish, whether or not it is on the agenda for the meeting. The Secretary attends all meetings of the Board and records the minutes. The Vice Chairman, Chief Financial Officer and General Counsel also attend meetings of the Board. Any one or all of these officers may be excused from all or any portion of a Board meeting at the request of any Director.

#### **Executive Sessions**

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The Board of Directors refers to meetings of the non-management Directors as executive sessions. The Presiding Director chairs executive sessions; however, he or she may choose to defer to a Committee Chair when the subject matter of the meeting falls within the purview of a Board Committee. The non-management Directors, led by the Presiding Director, determine the frequency, length and agenda for executive sessions. An executive session is scheduled immediately before or after a regular Board meeting at least twice each year; at least one of these sessions shall be held with only independent Directors participating.

### Site Visits

Directors are expected to visit Company facilities throughout the year. Periodically, the Board will meet away from the Company's headquarters in order to visit certain of the Company's operations and provide the Directors the opportunity to meet with local management.

### Information to be distributed prior to Meetings

Information regarding the Company's business and performance is distributed to all Directors on a monthly basis. In addition, business updates and information regarding recommendations for action by the Board at a meeting shall be made available to the Board a reasonable period of time before meetings.

### Functioning of Committees

#### Committee Structure

The Board believes that the Company benefits from its collective wisdom, and therefore the Board as a whole will deal with major corporate decisions. There are, however, certain key areas that require more in-depth examination than might be possible at a full Board meeting. Accordingly, the Board has established six standing Committees: Audit, Compensation, Corporate Responsibility, Executive, Finance and Governance. The Board may also establish *ad hoc* committees from time to time as circumstances and business activities warrant.

#### Committee Charters

Each standing Committee shall have a written charter that shall be approved by the full Board, upon the recommendation of the Governance Committee. Each Committee charter shall state the purpose of the Committee and reflect the responsibilities that the Committee has undertaken. Each Committee shall review its charter annually and recommend amendments to it as appropriate to reflect changes in the Committee's responsibilities, applicable law or regulations, and other relevant considerations.

#### Committee Membership

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Committees and their Chairs shall be appointed by the Board annually at the Annual Meeting of the Board, on recommendation of the Governance Committee. It is the Board's policy that, with the exception of the Executive Committee, only non-management Directors shall serve on the standing Committees. The members of the Audit, Compensation and Governance Committees shall at all times meet the requirements of applicable law and listing standards. It is the sense of the Board that it should benefit from the periodic rotation of Committee members and Committee Chairs, and the Governance Committee shall take this into account in its annual review of Committee membership.

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### **Committee Meetings**

The Chairs of the various Committees, in consultation with their Committee members, shall determine the frequency, length and agenda of Committee meetings. Information regarding matters to be considered at Committee meetings shall be distributed to Committee members a reasonable period of time before such meetings. The Chair of each Committee shall report on the activities of the Committee to the Board following Committee meetings, and minutes of Committee meetings shall be distributed to all Directors for their information.

### **Board Compensation and Share Ownership**

#### **Board Compensation**

Directors who are Company employees shall not be compensated for their services as Directors. The Governance Committee shall determine the form and amount of compensation for non-management Directors, including the non-executive Chairman, if applicable, subject to approval of the full Board of Directors. The Committee shall be sensitive to questions of independence that may be raised where Director fees and expenses exceed customary levels for companies of comparable scope and size.

#### **Share Ownership by Directors**

The Board of Directors believes that an alignment of Director interests with those of shareholders is important. All Directors are expected to own stock in the Company in accordance with the policy established by the Governance Committee.

#### **Leadership Development**

#### **Annual Review of Management Performance**

After consulting with the non-management Directors the Chairs of the Compensation and Governance Committees shall approve the annual goals and objectives of the CEO, which shall be consistent with the Company's goals and objectives relevant to the CEO's compensation established annually by the Compensation Committee in accordance with its Charter. In order to ensure alignment in these discussions and in evaluating the CEO's performance, the Chair of the Compensation Committee shall be a member of the Governance Committee. Each year, the Chairs of the Compensation and Governance Committees shall consult with the non-management Directors in evaluating the CEO's performance and shall thereafter jointly provide the CEO with a performance review for the preceding year. Consistent with this evaluation, the Compensation Committee shall establish the CEO's salary, bonus and other incentive and equity compensation for the year. In addition, the Compensation Committee shall also annually approve the compensation structure for the Company's officers, and shall approve the salary, bonus and other incentive and equity compensation for the Company's officers above the level of Vice President.

## **Succession Planning**

The Board shall annually consider a succession plan for the CEO and senior management.

## **Board Self-Evaluations**

The Governance Committee shall annually evaluate the performance of the Board of Directors as a whole. Individual Directors will be evaluated periodically, but in no event less often than each time they are slated for re-election. In completing these evaluations, the Governance Committee may choose to benchmark the practices of other boards of directors; circulate surveys, questionnaires and evaluation forms; hire outside consultants and advisors; and use such other methods as it may deem helpful and appropriate. At the conclusion of the evaluation process the Chair of the Governance Committee shall report the Committee's conclusions to the full Board and may make recommendations for improvement to the full Board.

## **Committee Self-Evaluations**

Each of the Audit, Compensation, and Governance Committees shall annually evaluate its performance as a Committee. Each of the Corporate Responsibility and Finance Committees shall periodically (at least every two years) evaluate its performance as a Committee. At the conclusion of the evaluation process, the Chair of each respective Committee shall report the Committee's conclusions to the full Board and may make recommendations for improvement to the full Board.

## **Director Orientation and Education**

New Directors shall participate in an orientation process, which shall address the Company's operations, performance, strategic plans, and corporate governance practices, and will include introductions to members of the Company's senior management and their respective responsibilities. All Directors are encouraged to participate in continuing education programs, and the Company shall pay the reasonable expenses of attendance by a Director at one such program per year.

## **Communications**

### **Access to Management and Information**

In order to fulfill their oversight responsibilities, Directors shall have free access to Company management and employees. The Board encourages the Chairman to invite members of management to make presentations at Board meetings in order to provide particular insights into aspects of the Company's business or to provide individuals with exposure to the Board for purposes of management development. Management shall be responsive to all requests for information from Board members.



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### **Board Interaction with Institutional Investors, the Press and Other Constituencies**

The Board believes that management speaks for the Company.

### **Public Communications with the Board**

The Board of Directors shall provide a means by which persons, including shareholders and employees, may communicate directly with non-management Directors with regard to matters relating to the Company's corporate governance and performance. The Board's independent Directors shall approve a process to be maintained by the Company's management for collecting and distributing communications with the Board. The means of communications with the Board shall be disclosed in the Company's annual proxy statement.

### **Shareholder Practices**

#### **Shareholder Nominations**

Shareholders may suggest Director candidates for consideration by the Governance Committee by writing to the Committee and providing the candidate's name, biographical data, qualifications and the candidate's written consent to be considered as a nominee and to serve as a Director if elected. Shareholders who wish to nominate Director candidates for election by shareholders at the Company's Annual Meeting of Shareholders may do so in accordance with the provisions for nomination described in the Company's By-Laws.

#### **Consideration of Shareholder Proposals**

The appropriate Board Committee will consider any proposal properly presented by a shareholder for inclusion in the Company's annual proxy statement. In considering the proposal, the Committee may seek input from an independent advisor and/or legal counsel, as appropriate, and will reach a conclusion and report to the full Board for its consideration. After full consideration by the Board of Directors, the shareholder proponent will be notified of the conclusion of the Board.

#### **Confidential Voting**

It is the Company's policy to protect the confidentiality of shareholder votes throughout the voting process. The policy in this regard shall be disclosed in the Company's annual proxy statement.

#### **Other Guidelines and Policies**



In addition to these Principles and the Committee charters, the Board and its Committees will from time to time establish operating procedures, guidelines and policies that pertain to their respective oversight functions. The Secretary of the Company is charged with maintaining copies of these guidelines and policies.

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***Appendix B. Standards on Director Independence***

As stated in McDonald's Corporation's Corporate Governance Principles, it is the policy of the Board of Directors that a substantial majority of Directors shall be independent of management. An independent Director is one who is free of any material relationship with the Company or its management. Each Director's independence status shall be disclosed annually in the proxy statement for the Annual Meeting of Shareholders.

The Board of Directors shall determine whether a Director is independent each year after reviewing pertinent facts and circumstances and taking into consideration all applicable laws, regulations and stock exchange listing requirements. In making its determination of independence, the Board of Directors shall also apply the following standards:

A Director who is an employee, or whose immediate family member is an executive officer, of the Company may not be deemed independent until three years after the end of such employment relationship. As used herein, "executive officer" has the same meaning as the term "officer" in Rule 16a-1(f) under the Securities Exchange Act of 1934.

A Director who receives, or whose immediate family member receives, more than \$100,000 during any 12-month period during the preceding three years in direct compensation from the Company, other than Director and Committee fees and deferred compensation for prior service (provided such compensation is not contingent in any way on continued service), may not be deemed independent. (Compensation received by an immediate family member for service as a non-executive employee of the Company will not be considered in determining independence under this test.)

A Director who is a partner or employee of a firm that is the Company's internal or external auditor may not be deemed independent.

A Director whose immediate family member is an employee of the Company's internal or external auditor and participates in that firm's audit, assurance or tax compliance (but not tax planning) practice may not be deemed independent.

A Director who was, or whose immediate family member was (but is no longer) a partner or employee of the Company's internal or external auditor firm and personally worked on the Company's audit within that time may not be deemed independent until three years after the end of such employment relationship.

A Director who is employed, or whose immediate family member is employed, as an executive officer of another company where any of the Company's current executive officers serve on that company's compensation committee may not be deemed independent until three years after the end of such service or the employment relationship.

A Director who is an executive officer or employee, or whose immediate family member is an executive officer, of a company (including a tax-exempt organization) that makes payments to, or receives payments from, the Company for property or services in an amount which, in any single fiscal year, exceeds the greater of \$1 million or 2% of such other company's consolidated gross revenues, may not be deemed independent until three years after falling below that threshold.

A Director who provides professional services (including, but not limited to, accounting, consulting, legal, investment banking or financial advisory services) to the Company within the preceding twelve-month period may not be deemed independent.

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Annual contributions made by the Company in excess of \$200,000 to any charitable, educational, civic or other tax-exempt organization (excluding those made under the Company's matching gift program) on which a Director serves as a director, trustee or executive officer will require consideration by the disinterested Directors and shall not be permitted if the contribution may impair, or appear to impair, the Director's ability to make independent judgments.

For purposes of these standards, the terms:

**Company** means McDonald's Corporation and any of its consolidated subsidiaries; and

**immediate family member** means a person's spouse, parents, children, siblings, mothers- and fathers-in-law, sons- and daughters-in-law, brothers- and sisters-in-law and anyone (other than domestic employees) sharing a person's home, but excluding any person who is no longer an immediate family member as a result of legal separation or divorce, or death or incapacitation.

To help maintain the independence of the Board, all Directors are required to deal at arm's length with the Company and to disclose circumstances material to the Director that might be perceived as a conflict of interest. As provided in the Corporate Governance Principles, if a change in circumstance affects an independent Director's continuing independence, that Director shall submit his or her resignation to the Chair of the Governance Committee. The Governance Committee shall determine whether to accept or reject such resignation.

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### **Appendix C. McDonald's Corporation Audit Committee Charter**

#### **I. Statement of Purpose**

The Audit Committee is a standing committee of the Board of Directors. The purpose of the Committee is to assist the Board of Directors in fulfilling its oversight responsibility relating to (i) the integrity of the Company's financial statements and financial reporting process and the Company's systems of internal accounting and financial controls; (ii) the performance of the internal audit services function; (iii) the annual independent audit of the Company's financial statements, the engagement of the independent auditors and the evaluation of the independent auditors' qualifications, independence and performance; (iv) the compliance by the Company with legal and regulatory requirements, including the Company's disclosure controls and procedures; (v) the evaluation of enterprise risk issues; and (vi) the fulfillment of the other responsibilities set out herein. The Committee shall also prepare the report of the Committee required to be included in the Company's annual proxy statement.

In discharging its responsibilities, the Committee is not itself responsible for the planning or conduct of audits or for any determination that the Company's financial statements are complete and accurate or in accordance with generally accepted accounting principles. This is the responsibility of management and the independent auditors.

#### **II. Organization**

A. *Charter.* At least annually, this charter shall be reviewed and reassessed by the Committee and any proposed changes shall be submitted to the Board of Directors for approval.

B. *Members.* The members of the Committee shall be appointed by the Board of Directors and shall meet the independence and experience requirements of applicable law, the listing standards of the New York Stock Exchange and applicable policies of the Board of Directors. The Committee shall be comprised of at least three members, at least one of whom shall meet the expertise requirements of the listing standards of the New York Stock Exchange. Committee members may be removed by the Board of Directors. The Board of Directors shall also designate a Committee Chairperson.

C. *Meetings.* In order to discharge its responsibilities, the Committee shall each year establish a schedule of meetings; additional meetings may be scheduled as required. In planning the annual schedule of meetings, the Committee shall ensure that sufficient opportunities exist for its members to meet separately with the independent auditors, the head of internal audit (and/or internal audit service providers) and management, and to meet in private with only the Committee members present.

D. *Agenda, Minutes and Reports.* An agenda, together with materials relating to the subject matter of each meeting, shall be sent to members of the Committee prior to each meeting. Minutes for all meetings of the Committee shall be prepared to document the Committee's discharge of its responsibilities. The minutes shall be circulated in draft form to all Committee members to ensure an accurate final record, shall be approved at a subsequent meeting of the Committee and shall be distributed periodically to the full Board of Directors. The Committee shall make regular reports to the Board of Directors.

E. *Performance Evaluation.* The Committee shall evaluate its performance on an annual basis and establish criteria for such evaluation.

### III. Responsibilities

The following shall be the principal responsibilities of the Audit Committee:

A. *Engagement of Independent Auditors.* The Committee shall directly appoint, retain, compensate, evaluate and terminate the Company's independent auditors. The Committee shall have the sole authority to approve all engagement fees to be paid to the independent auditors. The independent auditor shall report directly to the Committee.

B. *Determination as to Independence and Performance of Independent Auditors.* The Committee shall receive periodic reports from the independent auditors as required by the Independence Standards Board (or any successor body) regarding the auditors' independence, which shall be not less frequently than annually. The Committee shall discuss such reports with the auditors, and if so determined by the Committee, take appropriate action to satisfy itself of the independence of the auditors. The Committee shall review the performance of the Company's independent auditors annually. In doing so, the Committee shall consult with management and the Company's internal auditors and shall obtain and review a report by the independent auditors describing their internal control procedures, material issues raised by their most recent internal quality control review, or by any inquiry or investigation by governmental or professional authorities within the preceding five years and the response of the independent auditors. The Committee shall consider whether or not there should be a regular rotation of the lead audit partner or the independent audit firm. Any selection of the auditors by the Committee may be subject to shareholders' approval, as determined by the Board of Directors.

C. *Determination as to Performance of Internal Auditors.* With respect to any internal audit services that may be outsourced, the Committee shall be responsible for the engagement, evaluation and termination of the internal audit service providers and shall approve fees to be paid to the internal audit service providers. The Committee shall annually review the experience and qualifications of the senior members of the internal audit function and the quality control procedures of the internal auditors. As part of its responsibility to evaluate any internal audit service providers, the Committee shall review the quality control procedures applicable to the service providers. The Committee shall

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also obtain not less frequently than annually a report of the service providers addressing such service providers' internal control procedures, issues raised by their most recent internal quality control review or by any inquiry or investigation by governmental or professional authorities for the preceding five years and the response of the service providers.

*D. Audits by Internal and Independent Auditors.* The Committee shall discuss with the internal auditors, the internal audit service providers and the independent auditors the overall scope, plans and budget for their respective audits, including the adequacy of staffing and other factors that may affect the effectiveness and timeliness of such audits. In this connection, the Committee shall discuss with financial management, the internal audit service providers and the independent auditors the Company's major risk exposures (whether financial, operating or otherwise), the adequacy and effectiveness of the accounting and financial controls, and the steps financial management has taken to monitor and control such exposures and manage legal compliance programs, among other considerations that may be relevant to their respective audits. The Committee shall review with financial management and the independent auditors management's annual internal control report, including any attestation of same by the independent auditors. The internal audit service providers shall report periodically to the Committee regarding any significant deficiencies in the design or operation of the Company's internal controls, material weaknesses in internal controls and any fraud (regardless of materiality) involving persons having a significant role in the internal controls, as well as any significant changes in internal controls implemented by management during the most recent reporting period of the Company.

*E. Pre-Approval of Audit and Non-Audit Services.* The Committee shall establish and maintain guidelines for the retention of the independent auditors for any non-audit service and the fee for such service and shall determine procedures for the approval of audit and non-audit services in advance. The Committee shall, in accordance with such procedures, approve in advance any audit or non-audit service provided to the Company by the independent auditors, all as required by applicable law or listing standards.

*F. Review of Annual SEC Filings.* The Committee shall review with management and the independent auditors the Company's Annual Report on Form 10-K, including the disclosures under Management's Discussion and Analysis of Financial Condition and Results of Operations, their judgment about the quality, not just acceptability, of accounting principles, the reasonableness of significant judgments, the clarity of the disclosures in the financial statements and the adequacy of internal controls. The Committee shall also discuss the results of the annual audit and any other matters required to be communicated to the Committee by the independent auditors under generally accepted auditing standards, applicable law or listing standards, including matters required to be discussed by Statement on Auditing Standards No. 61, as amended by Statement on Auditing Standards No. 90. The Committee may discuss with the national office of the independent auditors issues on which it was consulted by the Company's audit team and matters of audit quality and consistency. Based on such review and discussion, the Committee shall make a determination whether to recommend to the Board of Directors that the audited financial statements be included in the Company's Form 10-K.

*G. Review of Quarterly SEC Filings and Other Communications.* The Committee shall meet to review and discuss with management and the independent auditors the quarterly financial information to be included in the Company's Quarterly Reports on Form 10-Q, including the disclosures under Management's Discussion and Analysis of Financial Condition and Results of Operations, and shall discuss any other matters required to be communicated to the Committee by the independent auditors under generally accepted auditing standards, applicable law or listing standards. The Committee shall also review and discuss the Company's earnings press releases as well as the types of financial information periodically provided to analysts and rating agencies. The Committee shall also discuss the results of the independent auditors review of the Company's quarterly financial information conducted in accordance with Statement on Auditing Standards No. 71.

*H. Review of Disclosure Controls and Procedures.* The Committee shall review with the Chief Executive Officer, the Chief Financial Officer and the General Counsel the Company's disclosure controls and procedures and shall review periodically, but in no event less frequently than quarterly, management's conclusions about the effectiveness of such disclosure controls and procedures, including any significant deficiencies in, or material non-compliance with, such controls and procedures.

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I. *Review of Certain Matters with Internal and Independent Auditors.* The Committee shall review periodically with financial management, the internal audit service providers and independent auditors the effect of new or proposed regulatory and accounting initiatives on the Company's financial statements and other public disclosures.

J. *Consultation with Independent Auditors.* The Committee shall review with the independent auditors any problems or difficulties the auditors may have encountered in connection with the annual audit or otherwise, any management letters provided to the Committee and the Company's responses. Such review shall address any difficulties encountered in the course of the audit work, including any restrictions on the scope of activities or access to required information, any disagreements with management regarding generally accepted accounting principles and other matters, material adjustments to the financial statements recommended by the independent auditors and adjustments that were proposed but passed, regardless of materiality.

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K. *Preparation of Report for Proxy Statement.* The Committee shall prepare the report required to be included in the Company's annual proxy statement, all in accordance with applicable rules and regulations.

L. *Employment of Former Audit Staff.* The Committee shall establish and maintain guidelines for the Company's hiring of former employees of the independent auditors, which shall meet the requirements of applicable law and listing standards.

M. *Whistleblowing Procedures.* The Committee shall establish and maintain procedures for the receipt, retention and treatment of complaints received by the Company regarding accounting, internal accounting controls or auditing matters and for the confidential, anonymous submission by employees of the Company of concerns regarding questionable accounting or auditing matters.

N. *Review of Legal and Regulatory Compliance.* The Committee shall periodically review with management, including the General Counsel, and the independent auditors any correspondence with, or other action by, regulators or governmental agencies and any employee complaints or published reports that raise concerns regarding the Company's financial statements, accounting or auditing matters or compliance with the Company's Standards of Business Conduct. The Committee shall also meet periodically, and may request to meet separately, with the General Counsel and other appropriate legal staff of the Company, and if appropriate, the Company's outside counsel, to review material legal affairs of the Company and the Company's compliance with applicable law and listing standards.

O. *Review of Certain Transactions with Directors and Related Parties.* The Committee shall review periodically, but no less frequently than annually, a summary of the Company's transactions with Directors and executive officers of the Company and with firms that employ Directors, as well as any other material related party transactions, for the purpose of recommending to the disinterested members of the Board of Directors that the transactions are fair, reasonable and within Company policy, and should be ratified and approved.

P. *Grant of Franchises.* The Committee shall approve the appropriateness of an initial grant of franchise(s) to a Company officer or a former Company officer in accordance with the Company's policy with regard to such grants of franchises. The Committee shall also approve the purchase of restaurants from a franchisee who immediately thereafter becomes a Company officer.

Q. *Review of Compliance Programs.* The Committee shall review annually with the General Counsel the adequacy and appropriateness of the Company's compliance programs. The review shall include a summary of employees' compliance with the Company's Standards of Business Conduct. The Committee shall be responsible for determining whether and on what terms to grant to any executive officer a waiver from the Company's Standards of Business Conduct.

R. *Access to Records, Consultants and Others.* The Committee shall have the full resources and authority (i) to investigate any matter brought to its attention with full access to all books, records, facilities and personnel of the Company; (ii) to retain outside legal, accounting or other consultants to advise the Committee; and (iii) to request any officer or employee of the Company, the Company's outside counsel, internal auditor, internal audit service providers or independent auditors to attend a meeting of the Committee or to meet with any members of, or consultants to, the Committee.

S. *Delegation.* The Committee may delegate any of its responsibilities to a subcommittee comprised of one or more members of the Committee. The Committee shall also carry out such other duties that may be delegated to it by the Board of Directors from time to time.



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### **Appendix D. McDonald's Corporation Compensation Committee Charter**

#### **I. Statement of Purpose**

The Compensation Committee is a standing committee of the Board of Directors. The Committee shall have the authority to determine the compensation of the Company's executive officers and such other employees as the Committee may decide. The Committee shall also prepare a report on executive compensation for inclusion in the Company's annual proxy statement.

#### **II. Organization**

A. *Charter.* At least annually, this charter shall be reviewed and reassessed by the Committee and any proposed changes shall be submitted to the Board of Directors for approval.

B. *Members.* The members of the Committee shall be appointed by the Board of Directors and shall meet the independence requirements of applicable law, the listing standards of the New York Stock Exchange and applicable policies of the Board of Directors. The Committee shall be comprised of at least three members. Committee members may be removed by the Board of Directors. The Board of Directors shall also designate a Committee Chairperson.

C. *Meetings.* In order to discharge its responsibilities, the Committee shall each year establish a schedule of meetings. Additional meetings may be scheduled as required.

D. *Agenda, Minutes and Reports.* The Chairperson of the Committee shall be responsible for establishing the agendas for meetings of the Committee. An agenda, together with materials relating to the subject matter of each meeting, shall be sent to members of the Committee prior to each meeting. Minutes for all meetings of the Committee shall be prepared to document the Committee's discharge of its responsibilities. The minutes shall be circulated in draft form to all Committee members to ensure an accurate final record, shall be approved at a subsequent meeting of the Committee and shall be distributed periodically to the full Board of Directors. The Committee shall make regular reports to the Board of Directors.

#### **III. Responsibilities**

The following shall be the principal responsibilities of the Committee:

A. *Compensation Philosophy and Program.* In consultation with senior management, the Committee shall establish the Company's general compensation philosophy, and oversee the development and implementation of executive compensation programs and policies with respect to the engagement of individuals as independent contractors of the Company. The Committee shall review on a periodic basis the Company's

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executive compensation programs and make any modifications that the Committee may deem necessary or advisable, in its sole discretion.

*B. Chief Executive Officer Compensation.* The Committee shall annually review and approve the Company's goals and objectives relevant to the compensation of the Chief Executive Officer and shall evaluate the performance of the Chief Executive Officer in light of those goals and objectives. Based on such evaluation, the Committee shall have the sole authority to set the compensation (including base salary, incentive compensation and equity-based awards) of the Chief Executive Officer. In determining incentive compensation, the Committee shall consider, among other factors it deems appropriate from time to time, the Company's performance and relative shareholder return, the value of similar incentive awards to chief executive officers at comparable companies, and the awards given to management in prior years.

*C. Officer Compensation.* The Committee shall also review and approve the compensation (including base salary, incentive compensation and equity-based awards) of officers above the level of Vice President of the Company and its business unit subsidiaries corresponding to its geographic operating segments, review and approve compensation guidelines for all other officers, and annually review the compensation of International Joint Venture Partners and Managing Directors.

*D. Benefit Plans.* The Committee shall review the terms of the Company's incentive compensation plans, equity-based plans, retirement plans, deferred compensation plans and welfare benefit plans. Unless otherwise delegated in accordance with the provisions of Article III.K., the Committee shall administer such plans, including determining any incentive or equity-based awards to be granted to members of senior management under any such plan.

*E. Post-Service Arrangements and Perquisites.* The Committee shall review periodically policies with respect to post-service arrangements and perquisites provided to officers, including the Chief Executive Officer.

*F. Appointment and Monitoring of Named Fiduciaries.* With respect to any funded employee benefit plan covering employees of the Company subject to the fiduciary responsibility provisions of the Employee Retirement Income Security Act of 1974, the Committee shall have the authority to appoint and terminate the named fiduciary or named fiduciaries of such plan and shall monitor their performance, unless such fiduciaries are specified in the constituent plan documents.

*G. Annual Compensation Committee Report.* The Committee shall produce an annual report on executive compensation for inclusion in the Company's annual proxy statement, all in accordance with applicable rules and regulations.

*H. Committee Performance Evaluation.* The Committee shall evaluate its own performance on an annual basis and develop criteria for such evaluation.

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I. *Access to Consultants.* The Committee shall have the resources and authority to discharge its duties and responsibilities as described herein, including the authority to select, retain and terminate counsel, consultants and other experts. The Committee shall have the sole authority to select, retain and terminate a compensation consultant and approve the consultant's fees and other retention terms.

J. *Delegation.* When appropriate, as permitted under applicable law and the listing standards of the New York Stock Exchange, the Board or the Committee may delegate any of its responsibilities to a subcommittee comprised of one or more members of the Committee, the Board or members of management.

K. *Other Duties.* The Committee shall also carry out such other duties as may be delegated to it by the Board of Directors from time to time.

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### **Appendix E. McDonald's Corporation Governance Committee Charter**

#### **I. Statement of Purpose**

The Governance Committee is a standing committee of the Board of Directors. The purpose of the Committee is to identify individuals qualified to become members of the Board, to recommend director nominees for each annual meeting of shareholders and nominees for election to fill any vacancies on the Board of Directors, to advise the Board with respect to the structure and composition of committees of the Board, and to address related matters. The Committee shall have the responsibility to recommend the compensation of the Company's Directors. The Committee shall also develop and recommend to the Board of Directors corporate governance principles and be responsible for leading the annual review of the Board's performance.

#### **II. Organization**

A. *Charter.* At least annually, this charter shall be reviewed and reassessed by the Committee and any proposed changes shall be submitted to the Board of Directors for approval.

B. *Members.* The members of the Committee shall be appointed by the Board of Directors and shall meet the independence requirements of applicable law, the listing standards of the New York Stock Exchange and applicable policies of the Board of Directors. The Committee shall be comprised of at least three members, one of whom shall be the Chair of the Board's Compensation Committee. Committee members may be removed by the Board of Directors. The Board of Directors shall also designate a Committee Chairperson.

C. *Meetings.* In order to discharge its responsibilities, the Committee shall each year establish a schedule of meetings; additional meetings may be scheduled as required.

D. *Agenda, Minutes and Reports.* The Chairperson of the Committee shall be responsible for establishing the agendas for meetings of the Committee. An agenda, together with materials relating to the subject matter of each meeting, shall be sent to members of the Committee prior to each meeting. Minutes for all meetings of the Committee shall be prepared to document the Committee's discharge of its responsibilities. The minutes shall be circulated in draft form to all Committee members to ensure an accurate final record, shall be approved at a subsequent meeting of the Committee and shall be distributed periodically to the full Board of Directors. The Committee shall make regular reports to the Board of Directors.

#### **III. Responsibilities**

The following shall be the principal responsibilities of the Committee:

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A. *Director Selection Criteria.* The Committee shall establish criteria for selecting new directors, which shall reflect, among other factors, a candidate's integrity and business ethics, strength of character, judgment, experience and independence, as well as factors relating to the composition of the Board, including its size and structure, the relative strengths and experience of current Board members and principles of diversity.

B. *Director Recruitment.* The Committee shall consider and recruit candidates to fill new positions on the Board of Directors and shall review any candidate recommended by the shareholders of the Company in accordance with the Company's By-Laws. As part of this responsibility, the Committee shall be responsible for conducting appropriate inquiries to establish such candidate's compliance with the independence and other qualification requirements established by the Committee.

C. *Consideration of Directors for Re-Election.* In connection with its annual recommendation of a slate of nominees, the Committee shall assess the contributions of those Directors slated for re-election, and shall at that time review its criteria for Board candidates in the context of the Board evaluation process and other perceived needs of the Board.

D. *Recommendation to Board.* The Committee shall recommend the director nominees for approval by the Board of Directors and the shareholders.

E. *Governance Principles.* The Committee shall recommend to the Board of Directors corporate governance principles addressing, among other matters, the size, composition and responsibilities of the Board of Directors and its committees, which shall be reviewed not less frequently than annually by the Committee. The Committee shall make recommendations to the Board of Directors with respect to changes to the corporate governance principles.

F. *Advice as to Committee Membership and Operations.* The Committee shall advise the Board of Directors with respect to the charters, structure and operations of the various committees of the Board of Directors and qualifications for membership thereon, including policies for rotation of members among committees of the Board of Directors.

G. *Evaluation of Board, Directors and Committee.* The Committee shall evaluate the performance of the Board of Directors on an annual basis. In discharging this responsibility, the Committee shall solicit comments from all Directors and report annually to the Board on its assessment of the Board's performance. The Committee shall periodically evaluate the performance of individual Directors. The Committee shall also evaluate its own performance on an annual basis and establish criteria for such evaluation.

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H. *Director Compensation.* The Committee shall recommend to the Board of Directors proposed changes in Board compensation, including retainer and meeting attendance fees, as well as other Director compensation program, and policies.

I. *Evaluation of Executive Management.* The Committee shall oversee the evaluation of executive management of the Company.

J. *Access to Records, Consultants and Others.* In discharging its responsibilities, the Committee shall have the resources and sole authority to engage any outside consultant or search firm to be used to identify director candidates for nomination to the Board of Directors, to retain outside consultants to advise the Committee and to approve the terms of any such engagement and the fees of any such consultant or search firm. The Committee shall have full access to any relevant records of the Company and may also request that any officer or other employee of the Company, the Company's outside counsel or any other person meet with any members of, or consultants to, the Committee.

K. *Delegation.* The Committee may delegate any of its responsibilities to a subcommittee comprised of one or more members of the Committee. The Committee shall also carry out such other duties that may be delegated to it by the Board of Directors from time to time.

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***Appendix F. Code of Conduct for the Board of Directors of McDonald's Corporation***

The members of the Board of Directors of McDonald's Corporation acknowledge and accept the scope and extent of our duties as Directors. We have a responsibility to carry out our duties in an honest and businesslike manner and within the scope of our authority, as set forth in the General Corporation Laws of the State of Delaware and in the Certificate of Incorporation and By-Laws of McDonald's Corporation. We are entrusted with and responsible for the oversight of the assets and business affairs of McDonald's Corporation in an honest, fair, diligent and ethical manner. As Directors we must act within the bounds of the authority conferred upon us and with the duty to make and enact informed decisions and policies in the best interests of McDonald's and its shareholders. The Board of Directors has adopted the following Code of Conduct and our Directors are expected to adhere to the standards of loyalty, good faith and the avoidance of conflict of interest that follow:

**Board Members will:**

Act in the best interests of, and fulfill their fiduciary obligations to, McDonald's shareholders;

Act honestly, fairly, ethically and with integrity;

Conduct themselves in a professional, courteous and respectful manner;

Comply with all applicable laws, rules and regulations;

Act in good faith, responsibly, with due care, competence and diligence, without allowing their independent judgment to be subordinated;

Act in a manner to enhance and maintain the reputation of McDonald's;

Disclose potential conflicts of interest that they may have regarding any matters that may come before the Board, and abstain from discussion and voting on any matter in which the Director has or may have a conflict of interest;

Make available to and share with fellow Directors information as may be appropriate to ensure proper conduct and sound operation of McDonald's and its Board of Directors;

Respect the confidentiality of information relating to the affairs of the Company acquired in the course of their service as Directors, except when authorized or legally required to disclose such information; and

Not use confidential information acquired in the course of their service as Directors for their personal advantage.

A Director who has concerns regarding compliance with this Code should raise those concerns with the Chairman of the Board and the Chairperson of the Governance Committee, who will determine what action shall be taken to deal with the concern. In the extremely unlikely event that a waiver of this Code for a Director would be in the best interest of the Company, it must be approved by the Governance Committee.



Directors will annually sign a confirmation that they have read and will comply with this Code.

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**Appendix G. McDonald's Corporation Code of Ethics for the Chief Executive Officer and Senior Financial Officers**

As the [specify office] of McDonald's Corporation (the Company), I acknowledge that the Company is committed to honesty and ethical conduct in all areas of its business and that officers with responsibility for the conduct or supervision of the Company's financial affairs play a special role in preserving and protecting shareholders' interests.

In furtherance of the above and to the best of my ability, I will adhere to the following principles and responsibilities:

Act at all times in accordance with the Company's Standards of Business Conduct, a copy of which has been provided to me and with which I will comply;

Act at all times with integrity, avoiding actual or apparent conflicts of interest in personal and professional relationships;

Address any apparent conflict of interest in personal and professional relationships in accordance with the highest ethical standards and promptly disclose to the General Counsel of the Company the nature of any such conflict of interest or any material transaction or relationship that reasonably could be expected to give rise to such a conflict of interest;

Provide, in the Company's reports filed with the Securities and Exchange Commission and other public communications, disclosure that is full, fair, accurate, complete, objective, timely and understandable;

Comply with applicable rules and regulations of all U.S. and non-U.S. governmental entities and other private and public regulatory agencies, including any exchanges on which the Company's securities may be listed;

Act in good faith, responsibly, with due care, competence and diligence, and without misrepresenting material facts or circumstances and without seeking improperly to influence or hinder the Company's independent auditors in any way in the performance of their engagement;

Act objectively, without allowing my independent judgment to be subordinated;

Maintain the confidentiality of Company information, except when authorized or otherwise required to make any disclosure, and avoid the use of any Company information for personal advantage;

Consistent with applicable law, share my knowledge with others within the Company to the extent appropriate to improve communications to the Company's shareholders and other constituents;

Keep abreast of emerging financial issues relevant to shareholders and other constituents;

Promote ethical behavior among employees under my supervision;

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Accept accountability for adherence to this Code of Ethics and the Company's Standards of Business Conduct; and

Achieve responsible use of and control over all assets and resources of the Company entrusted to me.

The Chief Executive Officer, the Chief Financial Officer and other senior financial officers will annually sign a confirmation that they have read and will comply with the Code.

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**Information about Attending the Annual Shareholders Meeting**

**Date**

Wednesday, May 11, 2005

**Time**

9:00 a.m. Central Time

**Place**

Prairie Ballroom

The Lodge

McDonald's Office Campus

Oak Brook, Illinois 60523

**Parking**

Limited parking is available on campus.

**Webcast**

Watch a live webcast of the Annual Shareholders Meeting by going to [www.investor.mcdonalds.com](http://www.investor.mcdonalds.com) and clicking Webcast. (A replay of the Annual Shareholders Meeting will be available for a limited time.)

**If you plan to attend**

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As seating in the Prairie Ballroom is very limited, we encourage shareholders to participate in the meeting via the live webcast. However, if you do decide to attend, please bring the tear-off portion of your proxy card or your brokerage statement reflecting your McDonald's holdings as proof of share ownership. Admission tickets will be given to shareholders on a first-come, first-served basis. Overflow rooms will be available for viewing the meeting. The registration desk will open at 7:30 a.m.

Please be aware that all items will be subject to inspection. Cameras and other recording devices will not be permitted at the meeting.

### **Directions**

*From downtown Chicago*

*(and near west suburbs)*

I-290 west (Eisenhower Expressway) to I-88 west (to Aurora). Exit I-88 at Cermak Road/22nd Street (first exit immediately after York Road tollbooth). At Cermak Road/22nd Street (stoplight), turn right. Go two stoplights to Jorie Boulevard, turn right. Go three stoplights to Kroc Drive, turn left. At stop sign, Ronald Lane, turn left. The Lodge is on left, parking is on right.

*From I-294*

*(south suburbs)*

I-294 north to I-88 west (to Aurora). Exit I-88 at Cermak Road/22nd Street (first exit immediately after York Road tollbooth). At Cermak Road/22nd Street (stoplight), turn right. Go two stoplights to Jorie Boulevard, turn right. Go three stoplights to Kroc Drive, turn left. At stop sign, Ronald Lane, turn left. The Lodge is on left, parking is on right.

*From O'Hare Airport / I-294*

*(north suburbs)*

I-294 south to I-88 west (to Aurora). Exit I-88 at Cermak Road/22nd Street (first exit immediately after York Road tollbooth). At Cermak Road/22nd Street (stoplight), turn right. Go two stoplights to Jorie Boulevard, turn right. Go three stoplights to Kroc Drive, turn left. At stop sign, Ronald Lane, turn left. The Lodge is on left, parking is on right.

*From I-355 North or South or I-88 West*

*(far west suburbs)*

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From either direction, take I-88 east (to Chicago). Exit at Midwest Road and turn left (stoplight). Take Midwest Road to 31st Street (stoplight), turn left. Take 31st Street to Jorie Boulevard (stoplight), turn left. Go to Kroc Drive (stoplight), turn right. At stop sign, Ronald Lane, turn left. The Lodge is on left, parking is on right.

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**Home Office**

McDonald's Corporation

McDonald's Plaza

Oak Brook, IL 60523

630-623-3000

[www.mcdonalds.com](http://www.mcdonalds.com)

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EXCEPT PER SHARE DATA**

	2004	2003	2002	2001	2000	1999	1998	1997	1996	1995	1994
Company-operated sales	\$ 14,224	12,795	11,500	11,041	10,467	9,512	8,895	8,136	7,571	6,863	5,793
Franchised and affiliated revenues	\$ 4,841	4,345	3,906	3,829	3,776	3,747	3,526	3,273	3,116	2,932	2,528
<b>Total revenues</b>	<b>\$ 19,065</b>	<b>17,140</b>	<b>15,406</b>	<b>14,870</b>	<b>14,243</b>	<b>13,259</b>	<b>12,421</b>	<b>11,409</b>	<b>10,687</b>	<b>9,795</b>	<b>8,321</b>
<b>Operating income</b>	<b>\$ 3,541<sup>(1)</sup></b>	<b>2,832<sup>(2)</sup></b>	<b>2,113<sup>(3)</sup></b>	<b>2,697<sup>(4)</sup></b>	<b>3,330</b>	<b>3,320</b>	<b>2,762<sup>(5)</sup></b>	<b>2,808</b>	<b>2,633</b>	<b>2,601</b>	<b>2,241</b>
<b>Income before taxes and cumulative effect of accounting changes</b>	<b>\$ 3,203<sup>(1)</sup></b>	<b>2,346<sup>(2)</sup></b>	<b>1,662<sup>(3)</sup></b>	<b>2,330<sup>(4)</sup></b>	<b>2,882</b>	<b>2,884</b>	<b>2,307<sup>(5)</sup></b>	<b>2,407</b>	<b>2,251</b>	<b>2,169</b>	<b>1,887</b>
<b>Net income</b>	<b>\$ 2,279<sup>(1)</sup></b>	<b>1,471<sup>(2,6)</sup></b>	<b>893<sup>(3,7)</sup></b>	<b>1,637<sup>(4)</sup></b>	<b>1,977</b>	<b>1,948</b>	<b>1,550<sup>(5)</sup></b>	<b>1,642</b>	<b>1,573</b>	<b>1,427</b>	<b>1,224</b>
<b>Cash provided by operations</b>	<b>\$ 3,904</b>	<b>3,269</b>	<b>2,890</b>	<b>2,688</b>	<b>2,751</b>	<b>3,009</b>	<b>2,766</b>	<b>2,442</b>	<b>2,461</b>	<b>2,296</b>	<b>1,926</b>
<b>Capital expenditures</b>	<b>\$ 1,419</b>	<b>1,307</b>	<b>2,004</b>	<b>1,906</b>	<b>1,945</b>	<b>1,868</b>	<b>1,879</b>	<b>2,111</b>	<b>2,375</b>	<b>2,064</b>	<b>1,539</b>
<b>Treasury stock purchases</b>	<b>\$ 605</b>	<b>439</b>	<b>687</b>	<b>1,090</b>	<b>2,002</b>	<b>933</b>	<b>1,162</b>	<b>765</b>	<b>605</b>	<b>321</b>	<b>500</b>
<b>Financial position at year end:</b>											
Total assets	\$ 27,838	25,838	24,194	22,535	21,684	20,983	19,784	18,242	17,386	15,415	13,592
Total debt	\$ 9,220	9,731	9,979	8,918	8,474	7,252	7,043	6,463	5,523	4,836	4,351
Total shareholders' equity	\$ 14,201	11,982	10,281	9,488	9,204	9,639	9,465	8,852	8,718	7,861	6,885
Shares outstanding <i>IN MILLIONS</i>	1,270	1,262	1,268	1,281	1,305	1,351	1,356	1,371	1,389	1,400	1,387
<b>Per common share:</b>											
Net income basic	\$ 1.81 <sup>(1)</sup>	1.16 <sup>(2,6)</sup>	.70 <sup>(3,7)</sup>	1.27 <sup>(4)</sup>	1.49	1.44	1.14 <sup>(5)</sup>	1.17	1.11	.99	.84
Net income diluted	\$ 1.79 <sup>(1)</sup>	1.15 <sup>(2,6)</sup>	.70 <sup>(3,7)</sup>	1.25 <sup>(4)</sup>	1.46	1.39	1.10 <sup>(5)</sup>	1.15	1.08	.97	.82
Dividends declared	\$ .55	.40	.24	.23	.22	.20	.18	.16	.15	.13	.12
Market price at year end	\$ 32.06	24.83	16.08	26.47	34.00	40.31	38.41	23.88	22.69	22.56	14.63
Company-operated restaurants	9,212	8,959	9,000	8,378	7,652	6,059	5,433	4,887	4,294	3,783	3,216
Franchised restaurants	18,248	18,132	17,864	17,395	16,795	15,949	15,086	14,197	13,374	12,186	10,944
Affiliated restaurants	4,101	4,038	4,244	4,320	4,260	4,301	3,994	3,844	3,216	2,330	1,739
<b>Total Systemwide restaurants</b>	<b>31,561</b>	<b>31,129</b>	<b>31,108</b>	<b>30,093</b>	<b>28,707</b>	<b>26,309</b>	<b>24,513</b>	<b>22,928</b>	<b>20,884</b>	<b>18,299</b>	<b>15,899</b>
<b>Franchised and affiliated sales<sup>(8)</sup></b>	<b>\$ 37,065</b>	<b>33,137</b>	<b>30,026</b>	<b>29,590</b>	<b>29,714</b>	<b>28,979</b>	<b>27,084</b>	<b>25,502</b>	<b>24,241</b>	<b>23,051</b>	<b>20,194</b>

<sup>(1)</sup> Includes pretax operating charges of \$130 million related to asset/goodwill impairment and \$160 million (\$21 million related to 2004 and \$139 million related to prior years) for a correction in the Company's lease accounting practices and policies (see Other operating expense, net note to the consolidated financial statements for further details), as well as a nonoperating gain of \$49 million related to the sale of the Company's interest in a U.S. real estate partnership, for a total pretax expense of \$241 million (\$172 million after tax or \$0.13 per share).

<sup>(2)</sup> Includes pretax charges of \$408 million (\$323 million after tax or \$0.25 per share) primarily related to the disposition of certain non-McDonald's brands and asset/goodwill impairment. See Other operating expense, net note to the consolidated financial statements for further details.

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- (3) *Includes pretax charges of \$853 million (\$700 million after tax or \$0.55 per share) primarily related to restructuring certain international markets and eliminating positions, restaurant closings/asset impairment and the write-off of technology costs. See Other operating expense, net note to the consolidated financial statements for further details.*
- (4) *Includes pretax operating charges of \$378 million primarily related to the U.S. business reorganization and other global change initiatives, and restaurant closings/asset impairment as well as net pretax nonoperating income of \$125 million primarily related to a gain on the initial public offering of McDonald's Japan, for a total pretax expense of \$253 million (\$143 million after tax or \$0.11 per share).*
- (5) *Includes pretax charges of \$322 million (\$219 million after tax or \$0.16 per share) consisting of \$162 million of Made For You costs and \$160 million related to a home office productivity initiative.*
- (6) *Includes a \$37 million after-tax charge (\$0.03 per share) to reflect the cumulative effect of the adoption of SFAS No. 143 Accounting for Asset Retirement Obligations, which requires legal obligations associated with the retirement of long-lived assets to be recognized at their fair value at the time the obligations are incurred. See Summary of significant accounting policies note to the consolidated financial statements for further details.*
- (7) *Includes a \$99 million after-tax charge (\$0.08 per share basic and \$0.07 per share diluted) to reflect the cumulative effect of the adoption of SFAS No. 142 Goodwill and Other Intangible Assets, which eliminates the amortization of goodwill and instead subjects it to annual impairment tests. See Summary of significant accounting policies note to the consolidated financial statements for further details. Adjusted for the nonamortization provisions of SFAS No. 142, net income per common share would have been \$0.02 higher in 2001 and 2000 and \$0.01 higher in 1999-1996.*
- (8) *While franchised and affiliated sales are not recorded as revenues by the Company, management believes they are important in understanding the Company's financial performance because these sales are the basis on which the Company calculates and records franchised and affiliated revenues and are indicative of the financial health of the franchisee base.*

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### **Management's discussion and analysis of financial condition and results of operations**

#### **Overview**

#### **Description of the business**

The Company primarily operates and franchises McDonald's restaurants. In addition, the Company operates certain non-McDonald's brands that are not material to the Company's overall results. Of the more than 30,000 McDonald's restaurants in over 100 countries, more than 8,000 are operated by the Company, approximately 18,000 are operated by franchisees/licensees and about 4,000 are operated by affiliates. In general, the Company owns the land and building or secures long-term leases for restaurant sites regardless of who operates the restaurant. This ensures long-term occupancy rights and helps control related costs.

Revenues consist of sales by Company-operated restaurants and fees from restaurants operated by franchisees and affiliates. These fees primarily include rent, service fees and/or royalties that are based on a percent of sales, with specified minimum rent payments. Fees vary by type of site, amount of Company investment and local business conditions. These fees, along with occupancy and operating rights, are stipulated in franchise/license agreements that generally have 20-year terms.

The business is managed as distinct geographic segments: United States; Europe; Asia/Pacific, Middle East and Africa (APMEA); Latin America and Canada. In addition, throughout this report we present a segment entitled "Other" that includes non-McDonald's brands (e.g., Boston Market and Chipotle Mexican Grill). The U.S. and Europe segments each accounts for approximately 35% of total revenues. France, Germany and the United Kingdom account for about 65% of Europe's revenues; Australia, China and Japan (a 50%-owned affiliate accounted for under the equity method) account for over 45% of APMEA's revenues; and Brazil accounts for about 40% of Latin America's revenues. These seven markets along with the U.S. and Canada are referred to as "major markets" throughout this report and comprise approximately 70% of total revenues.

In analyzing business trends, management considers a variety of performance and financial measures including Systemwide sales growth, comparable sales growth, operating margins and returns.

Constant currency results exclude the effects of foreign currency translation and are calculated by translating current year results at prior year average exchange rates. Management reviews and analyzes business results in constant currencies and bases certain compensation plans on these results because the Company believes they better represent the underlying business trends.

Systemwide sales in this report include sales by all McDonald's and Other restaurants, whether operated by the Company, by franchisees or by affiliates. While sales by franchisees and affiliates are not recorded as revenues by the Company, management believes the information is important in understanding the Company's financial performance because it is the basis on which the Company calculates and records franchised and affiliated revenues and is indicative of the financial health of our franchisee base.

Comparable sales are a key performance indicator used within the retail industry and are indicative of acceptance of the Company's initiatives as well as local economic and consumer trends. Increases or decreases in comparable sales represent the percent change in constant currency sales from the same period in the prior year for all McDonald's restaurants in operation at least thirteen months.

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McDonald's reports on a calendar basis and therefore the comparability of the same month, quarter and year with the corresponding period of the prior year will be impacted by the mix of days. The number of weekdays, weekend days and timing of holidays in a given timeframe can have a positive or negative impact on comparable sales. The Company refers to this impact as the calendar shift/trading day adjustment. This impact varies geographically due to consumer spending patterns and has the greatest impact on monthly comparable sales and typically has minimal impact annually, with the exception of leap years, such as 2004, due to an incremental full day of sales.

Return on incremental invested capital (ROIIC) is a measure reviewed by management to determine the effectiveness of capital deployed. The one-year return is calculated by taking the increase in operating income plus depreciation and amortization between 2004 and 2003 (numerator) and dividing this by the weighted average of 2004 and 2003 adjusted cash used for investing activities (denominator). The calculation assumes an average exchange rate over the periods included in the calculation. In addition to the one-year ROIIC, management reviews this measure over longer time periods in assessing the effectiveness of capital deployed and in allocating capital to business units.

### **Strategic direction and financial performance**

In 2002, the Company's results reflected a focus on growth through adding new restaurants, with associated high levels of capital expenditures and debt financing. This strategy, combined with challenging economic conditions and increased competition in certain key markets, adversely affected results and returns on investment.

In 2003, the Company introduced a comprehensive revitalization plan to increase McDonald's relevance to today's consumers as well as improve our financial discipline. We redefined our strategy to emphasize growth through adding more customers to existing restaurants and aligned the System around our customer-focused Plan to Win. Designed to deliver operational excellence and leadership marketing, this Plan focuses on the five drivers of exceptional customer experiences—people, products, place, price and promotion.

The near-term goal of our revitalization plan was to fortify the foundation of our business. By year-end 2004, we substantially achieved this goal.

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We improved the taste of many of our core menu offerings and introduced products that have been well received by consumers such as new salad lines, breakfast and chicken offerings. We offered a variety of price options that appeal to a broad spectrum of consumers. We streamlined processes such as new product development and restaurant operations, improved our training programs, and implemented performance measures, including a restaurant review and measurement process, to enable and motivate restaurant employees to serve customers better. We have begun to remodel many of our restaurants to create more contemporary, welcoming environments. We also launched the *i'm lovin' it* marketing theme, which achieved high levels of consumer awareness worldwide and gained McDonald's recognition as 2004 Marketer of the Year by *Advertising Age* magazine.

Over the past two years, we have also exercised increased financial discipline; we paid down debt, reduced capital expenditures and reduced selling, general & administrative expenses as a percent of revenues. In addition, we returned a significant amount of excess cash to shareholders in the form of dividends and share repurchases.

For each quarter of 2004, McDonald's increased customer visits, improved margins and delivered double-digit growth in operating income and earnings per share. In addition, comparable sales were positive across all geographic segments during each and every quarter.

Our 2004 performance reflected the underlying strength of our U.S. business, which generated impressive sales and margin improvements for the second consecutive year. In Europe, our 2004 comparable sales for the year were 2.4%. This indicates that we are making progress toward revitalizing this important business segment, despite challenges in certain markets.

### *Highlights from the year included:*

Comparable sales increased 6.9% on top of a 2.4% increase in 2003.

Consolidated revenues increased 11% to a record high of \$19 billion. Excluding the positive impact of currency translation, revenues increased 7%.

Systemwide sales increased 12%. Excluding the positive impact of currency translation, Systemwide sales increased 8%.

Net income per common share totaled \$1.79, compared with \$1.15 in 2003.

Company-operated margins as a percent of sales improved 80 basis points progressing towards our goal of increasing Company-operated margins to the levels reached in the year 2000.

Cash from operations increased more than \$600 million to \$3.9 billion, primarily due to increased margins driven by higher sales at existing restaurants as well as stronger foreign currencies.

Capital expenditures increased to \$1.4 billion, with a higher percentage related to reinvestment in existing restaurants as compared with 2003.



Debt pay-down totaled more than \$800 million.

The annual dividend was increased 38%, to about \$700 million.

Share repurchases totaled about \$600 million.

ROIIC was 41% for 2004. The decrease in impairment and other charges included in the increase in operating income between 2004 and 2003 benefited the return 10 percentage points. (See attached exhibit to this report.)

## Outlook for 2005

The long-term goal of our revitalization plan was to create a differentiated customer experience one that builds brand loyalty and delivers sustainable, profitable growth for shareholders. Looking forward, consistent with that goal, we are targeting average annual Systemwide sales and revenue growth of 3% to 5%, average annual operating income growth of 6% to 7%, and annual returns on incremental invested capital in the high teens. These targets exclude the impact of foreign currency translation.

As we move into 2005, we continue to execute our restaurant review and measurement process through a combination of graded restaurant visits, anonymous mystery shops and customer surveys, and we are rewarding high service levels with special incentives.

We also continue to evolve our menu to remain relevant. In the U.S., Fruit N' Walnut Salads, as well as new, premium chicken sandwiches will be added to the menu, along with a new coffee blend. In Europe, we will introduce a range of new products. In Canada, Toasted Deli Sandwiches were introduced during the fourth quarter of 2004 and a similar product line is being launched in Australia in 2005. New products and branded everyday value remain a focus, as we continue to refresh our offerings and feature our EuroSaver Menu in several European markets, the Amazing Value Menu in Asia and the Dollar Menu in the U.S.

We continue our remodeling and rebuilding efforts and are enhancing our convenience with initiatives such as extended hours.

Another priority in 2005 is our continued focus on the well-being of our customers. We plan to build on the progress made last year through menu choice, providing education and information about our food, and encouraging physical activity through various programs and partnerships. This year we will leverage our size, reach, and resources to positively impact millions of families worldwide.

We are confident in our plans for 2005. At the same time, we recognize the challenges we face. For example, we must continue to deliver solid results in the U.S., a very competitive marketplace, despite difficult sales comparisons. We believe that the combination of initiatives that benefited our U.S. business in 2004 along with new products will continue to create positive momentum in 2005.

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Outside the U.S., we must build on successes in some markets and overcome challenges in others. Notably, some key markets must increase consumer relevance, while others must build the business despite economic challenges. We believe that we are in a better position to overcome these issues today than we have been for some time. For example, in 2005 we sent 20 million households in the U.K. a brand book that combines value offers with important information designed to educate our customers about our product quality, balanced choices and social responsibility efforts. Additionally, we introduced a value menu in Germany, an economically challenged market, with heavy advertising support. Our plan is to leverage successes in markets, such as the U.S., Australia and France, to improve results in other countries.

In light of Chipotle Mexican Grill's strong performance and growing popularity, we are exploring strategic alternatives to fuel growth of this emerging fast-casual brand, which currently operates more than 400 restaurants. We believe Chipotle's value and potential might be maximized through alternative strategies that could include raising additional equity capital in public or private markets. This would have an additional benefit of enabling us to allocate more resources to growing sales and profits at existing McDonald's restaurants.

While the Company does not provide specific guidance on earnings per share, the following information is provided to assist in analyzing the Company's results.

Changes in constant currency Systemwide sales are driven by changes in comparable sales and restaurant unit expansion. The Company expects net restaurant additions to add slightly more than 1 percentage point to sales growth in 2005 (in constant currencies). Most of this anticipated growth will result from restaurants opened in 2004.

The Company does not provide specific guidance on changes in comparable sales. However, as a perspective, assuming no change in cost structure, a 1 percentage point increase in U.S. comparable sales would increase annual earnings per share by about 2 cents. Similarly, an increase of 1 percentage point in Europe's comparable sales would increase annual earnings per share by about 1.5 cents.

The Company expects full-year 2005 selling, general & administrative expenses to be relatively flat or to increase slightly in constant currencies and to decline as a percent of revenues and Systemwide sales, compared with 2004.

A significant part of the Company's operating income is from outside the U.S., and about 70% of its total debt is denominated in foreign currencies. Accordingly, earnings are affected by changes in foreign currency exchange rates, particularly the Euro and the British Pound. If the Euro and the British Pound both move 10% in the same direction (compared with 2004 average rates), the Company's annual earnings per share would change about 6 cents to 7 cents. In 2004, foreign currency translation benefited earnings per share by 6 cents due primarily to the Euro and the British Pound.

For 2005, the Company expects its net debt principal repayments to be approximately \$600 million to \$800 million. At the end of 2004, McDonald's debt-to-capital ratio was 39%. We plan to maintain a debt-to-capital ratio of 35% to 40% in the near term. The Company expects interest expense to be relatively flat in 2005 compared with 2004, based on current interest and foreign currency exchange rates and after considering net repayments.

The Company expects capital expenditures for 2005 to be approximately \$1.7 billion, reflecting higher investment in existing restaurants and stronger foreign currencies.

The Company expects to return at least \$1.3 billion to shareholders through dividends and share repurchases in 2005.

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The Company plans to adopt Financial Accounting Standards Board (FASB) Statement 123(R), *Share-Based Payment*, during first quarter 2005 and restate prior periods. Partly in anticipation of these new accounting rules, the Company modified its compensation plans to limit eligibility to receive share-based compensation and shifted a portion of share-based compensation to primarily cash-based incentive compensation. We expect the 2005 impact of the adoption of Statement 123(R) combined with the modifications to the Company's compensation plans to be about \$0.10 per share of expense.

A number of factors can affect our business, including the effectiveness of operating initiatives and changes in global and local business and economic conditions. These and other risks are noted under Forward-looking statements at the end of Management's discussion and analysis.

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**Table of Contents****Consolidated operating results***Operating results*

<i>DOLLARS IN MILLIONS, EXCEPT PER SHARE DATA</i>	2004		2003		2002
	Amount	Increase/ (decrease)	Amount	Increase/ (decrease)	Amount
<b>Revenues</b>					
Sales by Company-operated restaurants	\$ 14,224	11%	\$ 12,795	11%	\$ 11,500
Revenues from franchised and affiliated restaurants	4,841	11	4,345	11	3,906
<b>Total revenues</b>	<b>19,065</b>	<b>11</b>	<b>17,140</b>	<b>11</b>	<b>15,406</b>
<b>Operating costs and expenses</b>					
Company-operated restaurant expenses	12,100	10	11,006	11	9,907
Franchised restaurants occupancy expenses	1,003	7	938	12	840
Selling, general & administrative expenses	1,980	8	1,833	7	1,713
Other operating expense, net	441	(17)	531	(36)	833
<b>Total operating costs and expenses</b>	<b>15,524</b>	<b>8</b>	<b>14,308</b>	<b>8</b>	<b>13,293</b>
<b>Operating income</b>	<b>3,541</b>	<b>25</b>	<b>2,832</b>	<b>34</b>	<b>2,113</b>
Interest expense	358	(8)	388	4	374
Nonoperating (income) expense, net	(20)	nm	98	27	77
<b>Income before provision for income taxes and cumulative effect of accounting changes</b>	<b>3,203</b>	<b>36</b>	<b>2,346</b>	<b>41</b>	<b>1,662</b>
Provision for income taxes	924	10	838	25	670
<b>Income before cumulative effect of accounting changes</b>	<b>2,279</b>	<b>51</b>	<b>1,508</b>	<b>52</b>	<b>992</b>
Cumulative effect of accounting changes, net of tax*		nm	(37)	nm	(99)
<b>Net income</b>	<b>\$ 2,279</b>	<b>55%</b>	<b>\$ 1,471</b>	<b>65%</b>	<b>\$ 893</b>
<b>Per common share-diluted:</b>					
<b>Income before cumulative effect of accounting changes</b>	<b>\$ 1.79</b>	<b>52%</b>	<b>\$ 1.18</b>	<b>53%</b>	<b>\$ .77</b>
Cumulative effect of accounting changes*		nm	(.03)	nm	(.07)
<b>Net income</b>	<b>\$ 1.79</b>	<b>56%</b>	<b>\$ 1.15</b>	<b>64%</b>	<b>\$ .70</b>
<b>Weighted average common shares outstanding diluted</b>	<b>1,273.7</b>		<b>1,276.5</b>		<b>1,281.5</b>

\* See Cumulative effect of accounting changes for further discussion.

*nm Not meaningful.*

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**Table of Contents****Impairment and other charges, net**

The Company recorded charges associated with certain strategic actions, as well as from annual goodwill and asset impairment testing in 2004, 2003 and 2002. These charges generally represent actions or transactions related to the implementation of strategic initiatives of the Company, items that are unusual or infrequent in nature (such as the dispositions of certain non-McDonald's brands in 2003), charges resulting from impairment testing and a lease accounting correction in 2004. McDonald's management does not include these items when reviewing business performance trends because we do not believe these items are indicative of expected ongoing results.

On a pretax basis, the Company recorded \$241 million of impairment and other charges (net) in 2004, \$408 million of impairment and other charges in 2003 and \$853 million of impairment and other charges in 2002. All items were recorded in other operating expense with the exception of the gain related to the sale of the Company's interest in a U.S. real estate partnership during 2004, which was recorded in nonoperating income.

*Impairment and other charges (income)/expense*

<i>IN MILLIONS, EXCEPT PER SHARE DATA</i>	Pretax			After tax <sup>(3)</sup>			Per common share diluted		
	2004	2003	2002	2004	2003	2002	2004	2003	2002
Restaurant closings/impairment <sup>(1)</sup>	\$ 130	\$ 136	\$ 402	\$ 116	\$ 140	\$ 336	\$ .09	\$ .11	\$ .26
Restructuring		272	267		183	244		.14	.19
Lease accounting correction:									
Current year's impact	21			13			.01		
Prior years' impact	139			92			.07		
Other:									
Operating			184			120			.10
Nonoperating	(49)			(49)			(.04)		
<b>Total<sup>(2)</sup></b>	<b>\$ 241</b>	<b>\$ 408</b>	<b>\$ 853</b>	<b>\$ 172</b>	<b>\$ 323</b>	<b>\$ 700</b>	<b>\$ .13</b>	<b>\$ .25</b>	<b>\$ .55</b>

<sup>(1)</sup> Although restaurant closings occur each year, the restaurant closing charges in 2003 and 2002, discussed below, were the result of separate intensive reviews by management in conjunction with other strategic actions.

<sup>(2)</sup> See Other operating expense, net note to the consolidated financial statements for a summary of the activity in the related liabilities, if any. The Company expects to use cash provided by operations to fund the remaining obligations, primarily related to leases.

<sup>(3)</sup> Certain items were not tax effected.

*Restaurant closings/asset impairment*

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In 2004, the Company recorded \$130 million of pretax charges for asset and goodwill impairment, primarily in South Korea driven by its significant decline in performance over the past few years.

In 2003, the Company recorded \$136 million of net pretax charges consisting of: \$148 million primarily related to asset/goodwill impairment in Latin America; \$30 million for about 50 restaurant closings associated with strategic actions in Latin America; and a \$42 million favorable adjustment to the 2002 charge for restaurant closings, primarily due to about 85 fewer closings than originally anticipated.

In 2002, the Company recorded \$402 million of pretax charges consisting of: \$302 million related to management's decision to close about 750 underperforming restaurants primarily in the U.S. and Japan; and \$100 million primarily related to the impairment of assets for certain existing restaurants in Europe and Latin America. Most of the restaurants identified for closing had negative cash flows and/or very low annual sales volumes. Also, in many cases they would have required significant capital investment to remain financially viable.

### *Restructuring*

In 2003, the Company recorded \$272 million of pretax charges consisting of: \$237 million related to the loss on the sale of Donatos Pizzeria, the closing of all Donatos and Boston Market restaurants outside the U.S. and the exit of a domestic joint venture with Fazoli's; and \$35 million related to revitalization plan actions of McDonald's Japan, including headcount reductions, the closing of Pret A Manger stores in Japan and the early termination of a long-term management services agreement. These actions were consistent with management's strategy of concentrating the Company's capital and resources on the best near-term opportunities and avoiding those that distract from restaurant-level execution.

In 2002, the Company initiated actions designed to optimize restaurant operations and improve the business and recorded \$267 million of net pretax charges consisting of: \$201 million related to the anticipated transfer of ownership in five countries in the Middle East and Latin America to developmental licensees and ceasing operations in two countries in Latin America; \$81 million primarily related to eliminating approximately 600 positions (about half of which were in the U.S. and half of which were in international markets), reallocating resources and consolidating certain home office facilities to control costs; and a \$15 million favorable adjustment to the 2001 restructuring charge due to lower employee-related costs than originally anticipated. Under the developmental license business structure, which the Company successfully employs in about 30 markets outside the U.S. (approximately 400 restaurants), the licensee owns the business, including the real estate interest. While the Company generally does not have any capital invested in these markets, it receives a royalty based on a percent of sales.

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**Table of Contents***Lease accounting correction*

Like other companies in the restaurant and retail industries, McDonald's recently reviewed its accounting practices and policies with respect to leasing transactions. Following this review and in consultation with its external auditors, McDonald's has corrected an error in its prior practices to conform the lease term used in calculating straight-line rent expense with the term used to amortize improvements on leased property. The result of the correction is primarily to accelerate the recognition of rent expense under certain leases that include fixed-rent escalations by revising the computation of straight-line rent expense to include these escalations for certain option periods. As the correction relates solely to accounting treatment, it does not affect McDonald's historical or future cash flows or the timing of payments under the related leases and its effect on the Company's current or prior years' earnings per share, cash from operations and shareholders' equity is immaterial. These adjustments primarily impact the U.S., China, Boston Market and Chipotle. Other markets were less significantly impacted, as many of the leases outside of the U.S. do not contain fixed-rent escalations. In 2005, we expect the rent expense related to this computation to be about \$25 million of which about 40% relates to non-McDonald's brands.

*Other*

In 2004, the Company recorded a nonoperating gain of \$49 million related to the sale of the Company's interest in a U.S. real estate partnership. As a result of this transaction, the Company was able to reverse a valuation allowance related to certain capital loss carryforwards (see Provision for income taxes in Management's discussion and analysis).

In 2002, the Company recorded \$184 million of pretax charges consisting of \$170 million primarily related to the write-off of software development costs as a result of management's decision to terminate a long-term technology project; and \$14 million primarily related to the write-off of receivables and inventory in Venezuela as a result of the temporary closure of all McDonald's restaurants due to a national strike. Although the terminated technology project was expected to deliver long-term benefits, it was no longer viewed as the best use of capital, as the anticipated Systemwide cost over several years was expected to be more than \$1 billion.

**Impact of foreign currencies on reported results**

While changing foreign currencies affect reported results, McDonald's lessens exposures, where practical, by financing in local currencies, hedging certain foreign-denominated cash flows, and purchasing goods and services in local currencies.

In 2004 and 2003, foreign currency translation had a positive impact on consolidated revenues, operating income and earnings per share due to the strengthening of several major currencies, primarily the Euro and British Pound. In 2002, foreign currency translation had a minimal impact on revenues as the stronger Euro and British Pound were offset by weaker Latin American currencies (primarily the Argentine Peso, Brazilian Real and Venezuelan Bolivar); however, operating income in 2002 was positively impacted by foreign currency translation primarily due to the stronger Euro and British Pound.

*Impact of foreign currency translation on reported results***Reported amount**



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<i>IN MILLIONS, EXCEPT PER SHARE DATA</i>				Currency translation benefit/(loss)		
	2004	2003	2002	2004	2003	2002
Revenues	\$ 19,065	\$ 17,140	\$ 15,406	\$ 779	\$ 886	\$ 15
Company-operated margins <sup>(1)</sup>	2,003	1,695	1,513	91	101	29
Franchised margins <sup>(1)</sup>	3,832	3,405	3,064	139	195	39
Selling, general & administrative expenses	1,980	1,833	1,713	(57)	(68)	8
Operating income	3,541	2,832	2,113	160	189	90
Income before cumulative effect of accounting changes	2,279	1,508	992	80	89	42
Net income	2,279	1,471	893	80	89	42
Per common share diluted:						
Income before cumulative effect of accounting changes	1.79	1.18	.77	.06	.07	.03
Net income	1.79	1.15	.70	.06	.07	.04

<sup>(1)</sup> Includes McDonald's restaurants only.

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**Table of Contents****Revenues**

In 2004, consolidated revenue growth was driven by positive performance in all segments as well as stronger foreign currencies. Consolidated revenue growth in 2003 was driven by stronger foreign currencies and strong performance in the U.S.

*Revenues*

<i>DOLLARS IN MILLIONS</i>	Amount			Increase/ (decrease)		Increase/(decrease) excluding currency translation	
	2004	2003	2002	2004	2003	2004	2003
<i>Company-operated sales:</i>							
U.S.	\$ 3,828	\$ 3,594	\$ 3,172	7%	13%	7%	13%
Europe	5,174	4,498	3,982	15	13	5	
APMEA	2,390	2,158	2,115	11	2	7	(3)
Latin America	933	774	696	21	11	21	20
Canada	730	632	505	16	25	8	11
Other	1,169	1,139	1,030	3	11	3	10
<b>Total</b>	<b>\$ 14,224</b>	<b>\$ 12,795</b>	<b>\$ 11,500</b>	<b>11%</b>	<b>11%</b>	<b>6%</b>	<b>6%</b>
<i>Franchised and affiliated revenues:</i>							
U.S.	\$ 2,697	\$ 2,445	\$ 2,251	10%	9%	10%	9%
Europe	1,563	1,377	1,154	14	19	3	1
APMEA	331	289	253	14	14	4	
Latin America	75	85	118	(12)	(28)	(10)	(20)
Canada	168	146	128	15	14	7	1
Other	7	3	2	nm	33	nm	33
<b>Total</b>	<b>\$ 4,841</b>	<b>\$ 4,345</b>	<b>\$ 3,906</b>	<b>11%</b>	<b>11%</b>	<b>7%</b>	<b>5%</b>
<i>Total revenues:</i>							
U.S.	\$ 6,525	\$ 6,039	\$ 5,423	8%	11%	8%	11%
Europe	6,737	5,875	5,136	15	14	4	
APMEA	2,721	2,447	2,368	11	3	7	(3)
Latin America	1,008	859	814	17	6	18	14
Canada	898	778	633	15	23	8	9
Other	1,176	1,142	1,032	3	11	3	11
<b>Total</b>	<b>\$ 19,065</b>	<b>\$ 17,140</b>	<b>\$ 15,406</b>	<b>11%</b>	<b>11%</b>	<b>7%</b>	<b>6%</b>

In the U.S., the increases in revenues in 2004 and 2003 were due to the combined strength of the strategic menu, marketing and service initiatives. Also, franchised and affiliated revenues increased at a higher rate than Company-operated sales due to a higher percentage of franchised restaurants throughout 2004 compared with 2003, while throughout 2003 there was a higher percentage of Company-owned

restaurants than in 2002.

In 2004, the increase in Europe's revenues was due to strong comparable sales in Russia, which is entirely Company-operated, and positive comparable sales in France, the U.K. and many other markets, partly offset by Germany's poor performance. In 2003, Europe's revenues reflected strong performance in Russia driven by expansion and positive comparable sales, along with expansion in France, partly offset by weak results in the U.K. and Germany.

In 2004, the increase in APMEA's revenues was due primarily to strong performance in China and Australia as well as positive comparable sales in many other markets, partly offset by poor performance in South Korea. In 2003, APMEA's revenues benefited from positive comparable sales in Australia and expansion in China, but were negatively affected by weak results in Hong Kong, South Korea and Taiwan, compounded by consumer concerns about Severe Acute Respiratory Syndrome (SARS) in several markets in the first half of the year.

In Latin America, revenues in 2004 and 2003 increased in constant currencies primarily due to a higher percentage of Company-operated restaurants and positive comparable sales, especially in 2004.

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The following tables present Systemwide sales growth rates and the increase or decrease in comparable sales.

*Systemwide sales*

	Increase/ (decrease)			Increase/(decrease) excluding currency translation		
	2004	2003	2002	2004	2003	2002
U.S.	10%	9%	1%	10%	9%	1%
Europe	14	18	11	4	2	5
APMEA	12	6	(3)	6	(2)	(3)
Latin America	13	(4)	(17)	13	4	4
Canada	15	17	1	7	4	2
Other		10	9		10	9
Total	12%	11%	2%	8%	5%	2%

*Comparable sales McDonald's restaurants*

	Increase/(decrease)		
	2004	2003	2002
U.S.	9.6%	6.4%	(1.5)%
Europe	2.4	(0.9)	1.0
APMEA	5.6	(4.2)	(8.5)
Latin America	13.0	2.3	1.0
Canada	5.4		(2.5)
Total	6.9%	2.4%	(2.1)%

**Operating margins**

Operating margin information and discussions relate to McDonald's restaurants only and exclude non-McDonald's brands.

*Company-operated margins*

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Company-operated margin dollars represent sales by Company-operated restaurants less the operating costs of these restaurants. Company-operated margin dollars increased \$308 million or 18% (13% in constant currencies) in 2004 and increased \$182 million or 12% (5% in constant currencies) in 2003. The constant currency increase in both periods was primarily due to strong comparable sales.

### *Company-operated margins McDonald's restaurants*

<b><i>IN MILLIONS</i></b>	<b>2004</b>	2003	2002
U.S.	<b>\$ 731</b>	\$ 635	\$ 507
Europe	<b>807</b>	708	631
APMEA	<b>264</b>	213	239
Latin America	<b>89</b>	47	66
Canada	<b>112</b>	92	70
<b>Total</b>	<b>\$ 2,003</b>	\$ 1,695	\$ 1,513

### ***PERCENT OF SALES***

U.S.	<b>19.1%</b>	17.7%	16.0%
Europe	<b>15.6</b>	15.7	15.9
APMEA	<b>11.0</b>	9.9	11.3
Latin America	<b>9.5</b>	6.1	9.4
Canada	<b>15.3</b>	14.6	13.7
<b>Total</b>	<b>15.3%</b>	14.5%	14.4%

Operating cost trends as a percent of sales were as follows: food & paper costs increased in 2004 and decreased in 2003, payroll costs decreased in 2004 and were flat in 2003, and occupancy & other operating decreased in 2004 and increased in 2003.

In the U.S., the Company-operated margin percent increased in 2004 primarily due to positive comparable sales, partly offset by higher commodity costs and higher staffing levels. The U.S. Company-operated margin percent increased in 2003 primarily due to positive comparable sales and lower payroll as a percent of sales due to improved productivity and lower wage inflation, partly offset by higher commodity costs.

In Europe, Russia's strong performance benefited the Company-operated margin percent for 2004 but was more than offset by weak performance in Germany and the U.K. as well as higher commodity costs for the segment. In 2003, Europe's Company-operated margin percent reflected weak performance in the U.K., partly offset by improved margin performance in Germany and France.

In APMEA, the Company-operated margin percent in 2004 reflected improved performance in Hong Kong, Australia and China and poor performance in South Korea. In 2003, the margin declined significantly due to concerns of SARS impacting sales in many markets, partly offset by the SARS-related sales tax relief received from the Chinese government.

In Latin America, the Company-operated margin percent for 2004 reflected improved performance, primarily in Brazil, Argentina and Venezuela. In 2003, results reflected difficult economic conditions in these markets.

*Franchised margins*

Franchised margin dollars represent revenues from franchised and affiliated restaurants less the Company's occupancy costs (rent and depreciation) associated with those sites. Franchised margin dollars represented more than 65% of the combined operating margins in 2004, 2003 and 2002. Franchised margin dollars increased \$427 million or 13% (8% in constant currencies) in 2004 and \$341 million or 11% (5% in constant currencies) in 2003.

*Franchised margins McDonald's restaurants*

<u>IN MILLIONS</u>	<u>2004</u>	<u>2003</u>	<u>2002</u>
U.S.	\$ 2,177	\$ 1,945	\$ 1,781
Europe	1,195	1,044	885
APMEA	284	248	217
Latin America	45	54	79
Canada	131	114	102
Total	<u>\$ 3,832</u>	<u>\$ 3,405</u>	<u>\$ 3,064</u>
<u>PERCENT OF REVENUES</u>			
U.S.	80.7%	79.5%	79.1%
Europe	76.5	75.8	76.7
APMEA	85.7	85.6	85.8
Latin America	60.1	64.3	66.9
Canada	78.0	78.2	79.2
Total	<u>79.3%</u>	<u>78.4%</u>	<u>78.5%</u>

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The consolidated franchised margin percent increased for 2004 but slightly declined in 2003. Both periods benefited from strong comparable sales but reflected higher occupancy costs, due in part to an increased proportion of leased sites.

**Selling, general & administrative expenses**

Consolidated selling, general & administrative expenses increased 8% in 2004 and 7% in 2003 (5% and 3% in constant currencies). The constant currency increases in 2004 and 2003 reflected higher performance-based incentive compensation. In addition, 2003 included severance and other costs associated with the strategic decision to reduce restaurant openings.

Selling, general & administrative expenses as a percent of revenues declined to 10.4% in 2004 compared with 10.7% in 2003 and 11.1% in 2002, and selling, general & administrative expenses as a percent of Systemwide sales declined to 3.9% in 2004 compared with 4.0% in 2003 and 4.1% in 2002. Management believes that analyzing selling, general & administrative expenses as a percent of Systemwide sales as well as revenues is meaningful because these costs are incurred to support Systemwide restaurants.

*Selling, general & administrative expenses*

<b>DOLLARS IN MILLIONS</b>	<b>Amount</b>			<b>Increase/ (decrease)</b>		<b>Increase/(decrease) excluding currency translation</b>	
	<b>2004</b>	<b>2003</b>	<b>2002</b>	<b>2004</b>	<b>2003</b>	<b>2004</b>	<b>2003</b>
U.S.	\$ 602	\$ 567	\$ 558	6%	2%	6%	2%
Europe	485	424	359	14	18	4	2
APMEA	189	173	158	9	10	4	2
Latin America	107	102	102	5		5	8
Canada	64	54	49	20	9	11	(3)
Other	96	115	114	(16)	1	(16)	
Corporate <sup>(1)</sup>	437	398	373	10	7	10	7
<b>Total</b>	<b>\$ 1,980</b>	<b>\$ 1,833</b>	<b>\$ 1,713</b>	<b>8%</b>	<b>7%</b>	<b>5%</b>	<b>3%</b>

<sup>(1)</sup> Corporate expenses consist of home office support costs in areas such as facilities, finance, human resources, information technology, legal, marketing, supply chain management and training.

**Other operating expense, net**

*Other operating (income) expense, net*

<i><b>IN MILLIONS</b></i>	<b>2004</b>	2003	2002
Gains on sales of restaurant businesses	<b>\$ (45)</b>	\$ (55)	\$ (114)
Equity in earnings of unconsolidated affiliates	<b>(60)</b>	(37)	(24)
Other expense:			
Impairment and other charges <sup>(1)</sup>	<b>130</b>	408	853
Prior years' lease accounting correction	<b>139</b>		
Other <sup>(2)</sup>	<b>277</b>	215	118
<b>Total</b>	<b>\$ 441</b>	\$ 531	\$ 833

<sup>(1)</sup> See Other operating expense, net note to the consolidated financial statements for a discussion of the charges and a summary of the activity in the related liabilities.

<sup>(2)</sup> Includes \$21 million for current year's impact of lease accounting correction.

#### *Gains on sales of restaurant businesses*

Gains on sales of restaurant businesses include gains from sales of Company-operated restaurants as well as gains from exercises of purchase options by franchisees with business facilities lease arrangements (arrangements where the Company leases the businesses, including equipment, to franchisees who have options to purchase the businesses). The Company's purchases and sales of businesses with its franchisees and affiliates are aimed at achieving an optimal ownership mix in each market. Resulting gains or losses are recorded in operating income because the transactions are a recurring part of our business.

#### *Equity in earnings of unconsolidated affiliates*

Equity in earnings of unconsolidated affiliates—businesses in which the Company actively participates but does not control—is reported after interest expense and income taxes, except for U.S. restaurant partnerships, which are reported before income taxes. The increase in 2004 was primarily due to stronger performance in the U.S. and improved results from our Japanese affiliate. The increase in 2003 was primarily due to strong results in the U.S.

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**Table of Contents***Other expense*

The following table presents impairment and other charges and lease accounting correction amounts included in other operating expense by segment for 2004, 2003 and 2002.

*Impairment and other charges*

<b>IN MILLIONS</b>	<b>U.S.</b>	<b>Europe</b>	<b>APMEA</b>	<b>Latin America</b>	<b>Canada</b>	<b>Other</b>	<b>Corporate</b>	<b>Consolidated</b>
<b>2004</b>								
Restaurant closings/impairment	\$ 10	\$ 25	\$ 93	\$ 2				\$ 130
Lease accounting correction:								
Current year's impact	8		4			\$ 9		21
Prior years' impact	62	1	42		\$ 4	30		139
<b>Total</b>	<b>80</b>	<b>26</b>	<b>139</b>	<b>2</b>	<b>4</b>	<b>39</b>		<b>290</b>
Currency translation (loss)		(1)	(10)					(11)
<b>Total excluding currency translation</b>	<b>\$ 80</b>	<b>\$ 25</b>	<b>\$ 129</b>	<b>\$ 2</b>	<b>\$ 4</b>	<b>\$ 39</b>		<b>\$ 279</b>
<b>2003</b>								
Restaurant closings/impairment <sup>(1)</sup>	\$ (11)	\$ (20)	\$ 20	\$ 109	\$ (1)	\$ 29	\$ 10	\$ 136
Restructuring			35			237		272
<b>Total</b>	<b>(11)</b>	<b>(20)</b>	<b>55</b>	<b>109</b>	<b>(1)</b>	<b>266</b>	<b>10</b>	<b>408</b>
Currency translation benefit/(loss)		3	(5)	(20)		(11)		(33)
<b>Total excluding currency translation</b>	<b>\$ (11)</b>	<b>\$ (17)</b>	<b>\$ 50</b>	<b>\$ 89</b>	<b>\$ (1)</b>	<b>\$ 255</b>	<b>\$ 10</b>	<b>\$ 375</b>
<b>2002</b>								
Restaurant closings/impairment	\$ 74	\$ 135	\$ 81	\$ 62	\$ 4	\$ 31	\$ 15	\$ 402
Restructuring	25	9	141	66	2	3	21	267
Other		4		14	4		162	184
<b>Total</b>	<b>99</b>	<b>148</b>	<b>222</b>	<b>142</b>	<b>10</b>	<b>34</b>	<b>198</b>	<b>853</b>
Currency translation benefit/(loss)		(17)	(3)	23				3
<b>Total excluding currency translation</b>	<b>\$ 99</b>	<b>\$ 131</b>	<b>\$ 219</b>	<b>\$ 165</b>	<b>\$ 10</b>	<b>\$ 34</b>	<b>\$ 198</b>	<b>\$ 856</b>

<sup>(1)</sup> Bracketed amounts resulted from favorable adjustments to 2002 charges primarily due to fewer than anticipated restaurant closings.

In addition, other expense for 2004 reflected higher losses on asset dispositions, certain costs incurred to acquire restaurants operated by litigating franchisees in Brazil and provisions for certain contingencies, partly offset by lower provisions for uncollectible receivables in 2004 compared with 2003. Other expense in 2003 reflected higher losses on asset dispositions, higher provisions for uncollectible receivables and costs in the U.S. related to sites that will no longer be developed as a result of management's decision to significantly reduce capital expenditures.

**Operating income**

Consolidated operating income in 2004 and 2003 included higher combined operating margin dollars and higher selling, general & administrative expenses when compared with 2003 and 2002, respectively. In addition, 2003 included lower gains on sales of restaurant businesses when compared with 2002. In all three years, the Company recorded impairment and other charges that are included in these results.

*Operating income*

<i>DOLLARS IN MILLIONS</i>	Amount			Increase/ (decrease)		Increase/(decrease) excluding currency translation	
	2004	2003	2002	2004	2003	2004	2003
U.S.	\$ 2,182	\$ 1,982	\$ 1,673	10%	18%	10%	18%
Europe	1,471	1,339	1,022	10	31		13
APMEA	200	226	64	(11)	nm	(20)	nm
Latin America	(20)	(171)	(133)	89	(28)	91	(7)
Canada	178	163	125	9	30	2	15
Other	(16)	(295)	(66)	94	nm	94	nm
Corporate	(454)	(412)	(572)	(10)	28	(10)	28
<b>Total</b>	<b>\$ 3,541</b>	<b>\$ 2,832</b>	<b>\$ 2,113</b>	<b>25%</b>	<b>34%</b>	<b>19%</b>	<b>25%</b>

nm Not meaningful.

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In 2004 and 2003, U.S. operating income included higher combined operating margin dollars, partly offset by higher selling, general & administrative expenses and higher other operating expenses (excluding impairment charges and lease accounting correction), compared to 2003 and 2002, respectively.

Europe's constant currency results in 2004 benefited from strong performances in France and Russia as well as improved performance in Italy, offset by weak results in the U.K. Germany's performance weakened during the second half of 2004, and we expect the economic challenges there to continue to impact our performance in the near-term. In 2003, Europe's constant currency results also benefited from strong performance in France and Russia; however, difficult economic conditions in Germany and weak results in the U.K. negatively impacted results.

In APMEA, operating income in constant currencies for 2004 benefited from Australia's performance as well as improved performance in Hong Kong and China, partially offset by poor results in South Korea. APMEA's 2003 operating income reflected strong results in Australia. However, weak results in most other markets, compounded by concerns about SARS in certain markets, negatively impacted the segment.

In 2004, Latin America's operating loss decreased as compared with 2003, due to significantly lower provisions for uncollectible receivables and improved performance in Venezuela and Argentina. In addition, operating income in 2004 included certain costs incurred to acquire restaurants owned by litigating franchisees in Brazil. Latin America's operating income significantly declined in 2003 due to the continuing difficult economic conditions experienced by several key markets in the segment and significantly higher provisions for uncollectible receivables.

## **Interest expense**

Interest expense decreased in 2004 due to lower average debt levels and interest rates, partly offset by stronger foreign currencies. Interest expense increased in 2003 due to stronger foreign currencies, partly offset by lower average debt levels and interest rates.

## **Nonoperating (income) expense, net**

Nonoperating (income) expense includes miscellaneous income and expense items such as interest income, minority interests, and gains and losses related to other investments, financings and foreign currency translation.

Nonoperating (income) expense in 2004 included a gain of \$49 million related to the sale of the Company's interest in a U.S. real estate partnership as well as higher interest income. Nonoperating expense in 2003 reflected an \$11 million loss on the early extinguishment of debt as well as higher foreign currency translation losses compared with 2002.

## **Provision for income taxes**

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The following table presents the reported effective income tax rates as well as the effective income tax rates before impairment and other charges.

### *Effective income tax rates*

	2004	2003	2002
Reported effective income tax rates	<b>28.9%</b>	35.7%	40.3%
Impact of impairment and other charges, net <sup>(1)</sup>	<b>(0.1)</b>	(2.2)	(7.6)
Effective income tax rates before above charges	<b>28.8%</b>	33.5%	32.7%

<sup>(1)</sup> *Certain items were not tax effected.*

The effective income tax rate for the full year 2004 benefited from an international transaction and the utilization of certain previously unrealized capital loss carryforwards, both of which impacted 2004 only. In 2003 and 2002, the effective income tax rates were negatively impacted by certain asset impairment and other charges that were not tax effected, while 2004 has a lesser amount of such items.

Consolidated net deferred tax liabilities included tax assets, net of valuation allowance, of \$1,319 million in 2004 and \$1,032 million in 2003. Substantially all of the net tax assets arose in the U.S. and other profitable markets.

### **Cumulative effect of accounting changes**

Effective January 1, 2003, the Company adopted SFAS No.143, *Accounting for Asset Retirement Obligations*, which requires legal obligations associated with the retirement of long-lived assets to be recognized at their fair value at the time that the obligations are incurred. Effective January 1, 2002, the Company adopted SFAS No.142, *Goodwill and Other Intangible Assets*, which eliminates the amortization of goodwill and instead subjects it to annual impairment tests. See Summary of significant accounting policies note to the consolidated financial statements for further discussion.

### **Cash flows**

The Company generates significant cash from operations and has substantial credit capacity to fund operating and discretionary spending such as capital expenditures, debt repayments, dividends and share repurchase.

Cash from operations totaled \$3.9 billion and exceeded capital expenditures by \$2.5 billion in 2004, while cash from operations totaled \$3.3 billion and exceeded capital expenditures by \$2.0 billion in 2003. Cash provided by operations increased \$635 million in 2004 due to strong operating results, primarily in the U.S., and changes in working capital, partly offset by higher income tax payments. Cash provided by operations increased \$379 million in 2003 due to strong operating results, primarily in the U.S., partly offset by changes in working capital.

*Cash provided by operations*

<b><i>DOLLARS IN MILLIONS</i></b>	<b>2004</b>	2003	2002
Cash provided by operations	<b>\$ 3,904</b>	\$ 3,269	\$ 2,890
Cash provided by operations as a percent of capital expenditures	275%	250%	144%

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Cash used for investing activities totaled \$1.4 billion in 2004 due to higher capital expenditures and lower sales of property, offset by lower purchases of restaurant business. Cash used for investing activities also totaled \$1.4 billion in 2003, a decrease of \$1.1 billion compared with 2002 primarily due to lower capital spending as a result of fewer restaurant openings and fewer purchases of restaurant businesses.

Cash used for financing activities totaled \$1.6 billion in 2004, a decrease of \$103 million primarily due to higher pr