

OFFICE DEPOT INC
Form 10-Q
July 27, 2010
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UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-Q

(Mark One)

Quarterly Report Pursuant to Section 13 or 15 (d) of the
Securities Exchange Act of 1934
For the quarterly period ended June 26, 2010

or

Transition Report Pursuant to Section 13 or 15 (d) of the
Securities Exchange Act of 1934
For the transition period from _____ to _____

Commission file number 1-10948

Office Depot, Inc.

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

59-2663954
(I.R.S. Employer
Identification No.)

6600 North Military Trail; Boca Raton, Florida
(Address of principal executive offices)

33496
(Zip Code)

(561) 438-4800

(Registrant's telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report)

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

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

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

| | | | |
|-------------------------|-------------------------------------|---------------------------|--------------------------|
| Large accelerated filer | <input checked="" type="checkbox"/> | Accelerated filer | <input type="checkbox"/> |
| Non-accelerated filer | <input type="checkbox"/> | Smaller reporting company | <input type="checkbox"/> |

(Do not check if a smaller reporting company)

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

The number of shares outstanding of the registrant's common stock, as of the latest practicable date: At June 26, 2010 there were 275,959,210 outstanding shares of Office Depot, Inc. Common Stock, \$0.01 par value.

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Table of Contents**PART I. FINANCIAL INFORMATION****Item 1. Financial Statements****OFFICE DEPOT, INC.****CONDENSED CONSOLIDATED BALANCE SHEETS**

(In thousands, except share and per share amounts)

(Unaudited)

| | June 26, 2010 | December 26, 2009 | June 27, 2009 |
|--|------------------|----------------------|------------------|
| Assets | | | |
| Current assets: | | | |
| Cash and cash equivalents | \$ 577,840 | \$ 659,898 | \$ 558,710 |
| Receivables, net | 924,865 | 1,121,160 | 1,137,088 |
| Inventories | 1,176,018 | 1,252,929 | 1,264,355 |
| Deferred income taxes | 19,817 | 16,637 | 225,721 |
| Prepaid expenses and other current assets | 160,510 | 155,705 | 175,777 |
| Total current assets | 2,859,050 | 3,206,329 | 3,361,651 |
| Property and equipment, net | 1,230,351 | 1,277,655 | 1,316,286 |
| Goodwill | 19,431 | 19,431 | 19,431 |
| Other intangible assets | 22,782 | 25,333 | 26,725 |
| Deferred income taxes | 62,818 | 81,706 | 283,318 |
| Other assets | 325,710 | 279,892 | 259,229 |
| Total assets | \$ 4,520,142 | \$ 4,890,346 | \$ 5,266,640 |
| Liabilities and stockholders equity | | | |
| Current liabilities: | | | |
| Trade accounts payable | \$ 984,915 | \$ 1,081,381 | \$ 1,176,649 |
| Accrued expenses and other current liabilities | 1,123,461 | 1,280,296 | 1,101,177 |
| Income taxes payable | 18,109 | 6,683 | 20,508 |
| Short-term borrowings and current maturities of long-term debt | 66,158 | 59,845 | 62,484 |
| Total current liabilities | 2,192,643 | 2,428,205 | 2,360,818 |
| Deferred income taxes and other long-term liabilities | 593,054 | 654,851 | 668,369 |
| Long-term debt, net of current maturities | 656,995 | 662,740 | 669,273 |
| Total liabilities | 3,442,692 | 3,745,796 | 3,698,460 |
| Commitments and contingencies | | | |
| Redeemable preferred stock, net (liquidation preference \$368,516 in June 2010, \$368,116 in December 2009, and \$350,000 in June 2009) | 355,979 | 355,308 | 325,322 |
| Stockholders equity: | | | |
| Office Depot, Inc. stockholders equity: | | | |
| Common stock - authorized 800,000,000 shares of \$.01 par value; issued and outstanding shares 281,874,478 in 2010, 280,652,278 in December 2009 and | 2,819 | 2,807 | 2,807 |

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| | | | |
|--|--------------|--------------|--------------|
| 280,650,919 in June 2009 | | | |
| Additional paid-in capital | 1,187,301 | 1,193,157 | 1,203,521 |
| Accumulated other comprehensive income | 155,148 | 238,379 | 221,216 |
| Accumulated deficit | (570,215) | (590,195) | (130,541) |
| Treasury stock, at cost 5,915,268 shares in 2010, December 2009, and June 2009 | (57,733) | (57,733) | (57,733) |
| Total Office Depot, Inc. stockholders' equity | 717,320 | 786,415 | 1,239,270 |
| Noncontrolling interest | 4,151 | 2,827 | 3,588 |
| Total stockholders' equity | 721,471 | 789,242 | 1,242,858 |
| Total liabilities and stockholders' equity | \$ 4,520,142 | \$ 4,890,346 | \$ 5,266,640 |

This report should be read in conjunction with the Notes to Condensed Consolidated Financial Statements (Notes) herein and the Notes to Consolidated Financial Statements in the Office Depot, Inc. Form 10-K filed February 23, 2010 (the 2009 Form 10-K).

Table of Contents**OFFICE DEPOT, INC.****CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS****(In thousands, except per share amounts)****(Unaudited)**

| | 13 Weeks Ended | | 26 Weeks Ended | |
|---|--------------------|--------------------|------------------|---------------------|
| | June 26, 2010 | June 27, 2009 | June 26, 2010 | June 27, 2009 |
| Sales | \$ 2,699,475 | \$ 2,824,141 | \$ 5,771,445 | \$ 6,049,405 |
| Cost of goods sold and occupancy costs | 1,932,787 | 2,060,093 | 4,091,026 | 4,375,095 |
| Gross profit | 766,688 | 764,048 | 1,680,419 | 1,674,310 |
| Store and warehouse operating and selling expenses | 642,423 | 691,583 | 1,332,434 | 1,485,903 |
| General and administrative expenses | 151,861 | 170,394 | 320,078 | 346,793 |
| Operating profit (loss) | (27,596) | (97,929) | 27,907 | (158,386) |
| Other income (expense): | | | | |
| Interest income | 443 | 718 | 980 | 1,912 |
| Interest expense | (16,591) | (16,745) | (34,363) | (34,663) |
| Miscellaneous income (expense), net | 4,681 | 412 | 10,780 | (3,147) |
| Earnings (loss) before income taxes | (39,063) | (113,544) | 5,304 | (194,284) |
| Income tax benefit | (29,372) | (30,680) | (14,245) | (56,088) |
| Net earnings (loss) | (9,691) | (82,864) | 19,549 | (138,196) |
| Less: Net loss attributable to the noncontrolling interest | (206) | (792) | (434) | (1,385) |
| Net earnings (loss) attributable to Office Depot, Inc. | (9,485) | (82,072) | 19,983 | (136,811) |
| Preferred stock dividends | 9,213 | 486 | 18,688 | 486 |
| Income (loss) available to common shareholders | \$ (18,698) | \$ (82,558) | \$ 1,295 | \$ (137,297) |
| Earnings (loss) per share: | | | | |
| Basic | \$ (0.07) | \$ (0.31) | \$ | \$ (0.51) |

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| | | | |
|---------|--------|--------|--------|
| Diluted | (0.07) | (0.31) | (0.51) |
|---------|--------|--------|--------|

Weighted average number of common shares outstanding:

| | | | | |
|---------|---------|---------|---------|---------|
| Basic | 275,320 | 270,290 | 274,777 | 271,735 |
| Diluted | 275,320 | 270,290 | 274,777 | 271,735 |

This report should be read in conjunction with the Notes herein and the Notes to Consolidated Financial Statements in the 2009 Form 10-K.

Table of Contents**OFFICE DEPOT, INC.****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS****(In thousands)****(Unaudited)**

| | 26 Weeks Ended | |
|---|--------------------------|--------------------------|
| | June 26, 2010 | June 27, 2009 |
| Cash flows from operating activities: | | |
| Net earnings (loss) | \$ 19,549 | \$ (138,196) |
| Adjustments to reconcile net earnings (loss) to net cash provided by operating activities: | | |
| Depreciation and amortization | 103,581 | 106,796 |
| Charges for losses on inventories and receivables | 27,970 | 35,239 |
| Changes in working capital and other | (118,834) | 102,547 |
| Net cash provided by operating activities | 32,266 | 106,386 |
| Cash flows from investing activities: | | |
| Capital expenditures | (83,202) | (53,799) |
| Acquisition related payments | (10,952) | |
| Release of restricted cash | | 6,037 |
| Proceeds from assets sold and other | 17,746 | 148,746 |
| Net cash provided by (used in) investing activities | (76,408) | 100,984 |
| Cash flows from financing activities: | | |
| Proceeds from exercise of stock options and sale of stock under employee stock purchase plans | 1,119 | 34 |
| Tax benefits from employee share-based payments | 2,371 | |
| Proceeds from issuance of redeemable preferred stock, net | | 326,861 |
| Preferred stock dividends | (9,213) | |
| Share transactions under employee related plans | (1,244) | |
| Debt related fees | (4,688) | |
| Net payments on borrowings | (2,857) | (139,043) |
| Net cash provided by (used in) financing activities | (14,512) | 187,852 |
| Effect of exchange rate changes on cash and cash equivalents | (23,404) | 7,743 |
| Net increase (decrease) in cash and cash equivalents | (82,058) | 402,965 |
| Cash and cash equivalents at beginning of period | 659,898 | 155,745 |
| Cash and cash equivalents at end of period | \$ 577,840 | \$ 558,710 |

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This report should be read in conjunction with the Notes herein and the Notes to Consolidated Financial Statements in the 2009 Form 10-K.

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OFFICE DEPOT, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note A Summary of Significant Accounting Policies

Basis of Presentation: Office Depot, Inc., including consolidated subsidiaries, is a global supplier of office products and services. Fiscal years are based on a 52- or 53-week period ending on the last Saturday in December. The Condensed Consolidated Balance Sheet at December 26, 2009 has been derived from audited financial statements at that date. The condensed consolidated interim financial statements as of June 26, 2010 and June 27, 2009, and for the 13-week and 26-week periods ended June 26, 2010 (also referred to as the second quarter of 2010 and the first half of 2010) and June 27, 2009 (also referred to as the second quarter of 2009 and the first half of 2009) are unaudited. However, in our opinion, these financial statements reflect adjustments (consisting only of normal, recurring items) necessary to provide a fair presentation of our financial position, results of operations and cash flows for the periods presented. We have included the balance sheet from June 27, 2009 to assist in analyzing our company. The June 27, 2009 balance sheet includes a line for Deferred income taxes, separate from Other assets, to conform to the June 26, 2010 and December 26, 2009 presentation.

These interim results are not necessarily indicative of the results that should be expected for the full year. For a better understanding of Office Depot, Inc. and its condensed consolidated financial statements, we recommend reading these condensed interim financial statements in conjunction with the audited financial statements for the year ended December 26, 2009, which are included in our 2009 Annual Report on Form 10-K (the 2009 Form 10-K), filed with the U.S. Securities and Exchange Commission (SEC).

Cash Management: Our cash management process generally utilizes zero balance accounts which provide for the reimbursement of the related disbursement accounts on a daily basis. Accounts payable and accrued expenses as of June 26, 2010, December 26, 2009 and June 27, 2009 included \$51 million, \$77 million and \$87 million, respectively, of disbursements not yet presented for payment drawn in excess of our book deposit balances where offset provisions exist. We may borrow to meet working capital and other needs throughout any given quarter, which may result in higher levels of borrowings and invested cash within the period. At the end of the quarter, excess cash may be used to minimize borrowings outstanding at the balance sheet date.

New Accounting Pronouncements: There are no recently issued accounting standards that are expected to have a material effect on our financial condition, results of operations or cash flows.

Note B Debt

On March 26, 2010, the company executed a second amendment to its asset based credit facility. This second amendment amends the facility by, among other things, allowing the company to make certain restricted payments, including the payment of cash dividends on preferred stock and make share repurchases, in an aggregate amount of \$50 million per fiscal year, subject to the maintenance of certain minimum liquidity conditions, removing the ability of the company to elect one- or two-month interest periods with respect to its LIBOR borrowings, making certain technical amendments to permit the company to issue unsecured or subordinated convertible debt securities, allowing the company and its subsidiaries to enter into certain internal tax restructuring transactions subject in certain circumstances to various conditions, and waiving certain technical events of default, including written notice of certain events to the U.S. Agent and European Agent under the asset based credit facility and certain related security agreements. The company was in compliance with all applicable financial covenants at June 26, 2010.

Table of Contents**Note C Redeemable Preferred Stock**

In June 2009, the company issued \$350 million of Redeemable Convertible Preferred Stock with a 10% stated dividend rate. Dividends are payable quarterly and are paid in-kind or, in cash at the discretion of the board of directors, to the extent that the company has funds legally available for such payment. If not paid in cash, an amount equal to the cash dividend due will be added to the liquidation preference and measured for accounting purposes at fair value. Dividends accrued through January 1, 2010, were settled in-kind. Subsequent quarterly dividends of \$9.2 million were paid in cash on April 1, 2010 and July 1, 2010.

Note D Asset Impairments, Exit Costs and Other Charges

In prior years, we performed strategic reviews of assets and processes with the goal of positioning the company to deal with the degradation in the global economy and to benefit from its eventual improvement. The results of those internal reviews led to decisions to close stores, exit certain businesses and write off certain assets that were not seen as providing future benefit. These decisions resulted in material charges (the Charges) that were recognized during the fourth quarter of 2008 and fiscal year 2009. Our measurement of Division operating profit excludes the Charges because they are evaluated internally at the corporate level.

As of the end of 2009, we had substantially completed all activities falling under our strategic reviews. Although we did not recognize new Charges under these programs during the first half of 2010, positive and negative adjustments to previously accrued amounts as well as accretion on discounted long-term accruals such as lease obligations impacted our results in the period. Amortizations, settlements and adjustments related to existing accruals are included in store and warehouse operating and selling expenses and recognized at the corporate level.

During the second quarter of 2009, we recognized approximately \$35 million of Charges associated with these activities as the previously-identified plans were implemented and the related accounting recognition criteria were met. Approximately \$30 million is included in store and warehouse operating and selling expenses and \$5 million is included in general and administrative expenses on our Condensed Consolidated Statement of Operations. During the first half of 2009, we recognized Charges of approximately \$155 million, of which, \$126 million is included in store and warehouse operating and selling expenses, \$19 million is included in general and administrative expenses and \$10 million is included in cost of goods sold and occupancy costs. Implementation of these activities during the 2009 periods resulted in charges primarily for lease accruals, severance expenses and asset impairments related to sale-leaseback transactions that closed during the period.

During the first half of 2009, we also entered into several sale and sale-leaseback transactions related to the strategic review and to enhance liquidity. Total proceeds from these transactions were approximately \$147 million and are included in the investing section on our Condensed Consolidated Statement of Cash Flows. One transaction was the sale of an asset previously classified as a capital lease. Payments to satisfy the existing capital lease obligation are included in the financing section of the Condensed Consolidated Statement of Cash Flows. Losses on these transactions are included in the Charges above. Gains have been deferred and will reduce rent expense over the related leaseback periods. An additional sale and leaseback arrangement associated with operating properties included provisions that resulted in the transaction being accounted for as a financing.

Exit cost accruals related to the activities described above are as follows:

| (In millions) | Balance at December 26, 2009 | Cash payments | Accretion on lease obligations | Currency and other adjustments | Balance at June 26, 2010 |
|--------------------------------|------------------------------------|------------------|--------------------------------------|--------------------------------------|--------------------------------|
| One-time termination benefits | \$ 13 | \$ (10) | \$ 7 | \$ (1) | \$ 2 |
| Lease and contract obligations | 162 | (39) | 7 | (4) | 126 |
| Total | \$ 175 | \$ (49) | \$ 7 | \$ (5) | \$ 128 |

Table of Contents**Note E Stockholders Equity and Comprehensive Income**

The following table reflects the changes in stockholders' equity attributable to both Office Depot, Inc. and the noncontrolling interests of our subsidiaries in India, Sweden and South Korea, in which we have a majority, but not total, ownership interest.

| <i>(In thousands)</i> | Attributable to Office Depot, Inc. | Attributable to noncontrolling interest | Total |
|---|---|--|--------------|
| Stockholders' equity at December 26, 2009 | \$ 786,415 | \$ 2,827 | \$ 789,242 |
| Comprehensive income: | | | |
| Net earnings (loss) | 19,983 | (434) | 19,549 |
| Other comprehensive income (loss): | (83,231) | (359) | (83,590) |
| Comprehensive income (loss) | (63,248) | (793) | (64,041) |
| Capital contributions from noncontrolling interest | | 2,117 | 2,117 |
| Preferred stock dividends | (18,688) | | (18,688) |
| Share transactions under employee related plans | 2,246 | | 2,246 |
| Amortization of long-term incentive stock grants | 10,595 | | 10,595 |
| Stockholders' equity at June 26, 2010 | \$ 717,320 | \$ 4,151 | \$ 721,471 |
| Stockholders' equity at December 27, 2008 | \$ 1,362,950 | \$ 4,883 | \$ 1,367,833 |
| Comprehensive income: | | | |
| Net earnings (loss) | (136,811) | (1,385) | (138,196) |
| Other comprehensive income (loss): | 4,019 | 90 | 4,109 |
| Comprehensive income (loss) | (132,792) | (1,295) | (134,087) |
| Share transactions under employee and direct stock purchase plans | (4,398) | | (4,398) |
| Amortization of long-term incentive stock grants | 13,510 | | 13,510 |
| Stockholders' equity at June 27, 2009 | \$ 1,239,270 | \$ 3,588 | \$ 1,242,858 |

Comprehensive income included all non-owner changes in stockholders' equity and consists of the following:

| <i>(In thousands)</i> | Second Quarter | | First Half | |
|---|-----------------------|-------------|-------------------|--------------|
| | 2010 | 2009 | 2010 | 2009 |
| Net earnings (loss) | \$ (9,691) | \$ (82,864) | \$ 19,549 | \$ (138,196) |
| Other comprehensive income (loss), net of tax where applicable: | | | | |
| Foreign currency translation adjustments | (48,042) | 52,180 | (86,069) | 5,008 |
| Amortization of gain on cash flow hedge | (414) | (414) | (829) | (829) |
| Change in deferred pension | 3,643 | (2,806) | 4,614 | (2,806) |
| Change in deferred cash flow hedge | (1,411) | 1,742 | (1,309) | 2,736 |
| Other | (434) | | 3 | |
| Total other comprehensive income (loss), net of tax, where applicable | (46,658) | 50,702 | (83,590) | 4,109 |
| Comprehensive income (loss) | (56,349) | (32,162) | (64,041) | (134,087) |

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| | | | | |
|---|-------------|-------------|-------------|--------------|
| Less: comprehensive income (loss) attributable to the noncontrolling interest | (538) | (587) | (793) | (1,295) |
| Comprehensive income (loss) attributable to Office Depot, Inc. | \$ (55,811) | \$ (31,575) | \$ (63,248) | \$ (132,792) |

Table of Contents**Note F Earnings Per Share**

The following table represents the calculation of net earnings (loss) per common share:

| <i>(In thousands, except per share amounts)</i> | Second Quarter | | First Half | |
|---|-----------------------|-------------|-------------------|--------------|
| | 2010 | 2009 | 2010 | 2009 |
| Basic Earnings Per Share | | | | |
| Numerator: | | | | |
| Income (loss) available to common shareholders | \$ (18,698) | \$ (82,558) | \$ 1,295 | \$ (137,297) |
| Denominator: | | | | |
| Weighted-average shares outstanding | 275,320 | 270,290 | 274,777 | 271,735 |
| Basic earnings (loss) per share | \$ (0.07) | \$ (0.31) | \$ | \$ (0.51) |
| Diluted Earnings Per Share | | | | |
| Numerator: | | | | |
| Income (loss) available to common shareholders | \$ (18,698) | \$ (82,558) | \$ 1,295 | \$ (137,297) |
| Preferred stock dividends | 9,213 | 486 | 18,688 | 486 |
| Net earnings (loss) for calculation | \$ (9,485) | \$ (82,072) | \$ 19,983 | \$ (136,811) |
| Denominator: | | | | |
| Weighted-average shares outstanding | 275,320 | 270,290 | 274,777 | 271,735 |
| Effect of dilutive securities: | | | | |
| Stock options and restricted stock | 5,567 | 3,416 | 5,970 | 1,740 |
| Redeemable preferred stock | 73,703 | 3,851 | 73,650 | 1,926 |
| Diluted weighted-average shares outstanding | 354,590 | 277,557 | 354,397 | 275,401 |
| Diluted earnings (loss) per share | N/A | N/A | N/A | N/A |

Following the issuance of the redeemable preferred stock in 2009, basic earnings per share is computed after consideration of preferred stock dividends. Diluted earnings per share is based on earnings before preferred stock dividends, but after assumed conversion into common stock unless such computation results in a number that is less dilutive. The diluted share amounts are provided for informational purposes, as basic earnings (loss) per share is the most dilutive for the periods presented.

The preferred stock dividends payable on July 1, 2010 and April 1, 2010 were paid in cash. Prior dividends were paid in-kind and a separate determination of fair value above the stated dividend rate was required for those periods. The valuation reduced basic earnings per share in the respective periods, but because the company reported losses, was antidilutive in the diluted earnings per share calculation and therefore not applicable. Shares of redeemable preferred stock have certain participation rights with common stock. A two class security earnings per share presentation will be provided for any period in which these rights impact the earnings per share calculation.

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Awards of options and nonvested shares representing approximately 15.2 million and 13.7 million additional shares of common stock were outstanding for the second quarter and first half of 2010, respectively, but were not included in the computation of diluted earnings per share because their effect would have been antidilutive. Also, the calculated effect of dilutive securities under relevant accounting rules includes a tax benefit from assumed employee share-based awards. That assumed benefit may be limited in future periods, depending on available carryback and carryforward deductions by tax jurisdiction. If all assumed tax benefits were removed from the calculation, the diluted weighted-average share amount would increase approximately 2.4 million shares at June 26, 2010.

Note G Division Information

Office Depot operates in three segments: North American Retail Division, North American Business Solutions Division, and International Division. The following is a summary of our significant accounts and balances by segment (or Division), reconciled to consolidated totals.

| <i>(In thousands)</i> | Sales | | | |
|--|----------------|--------------|--------------|--------------|
| | Second Quarter | | First Half | |
| | 2010 | 2009 | 2010 | 2009 |
| North American Retail Division | \$ 1,100,894 | \$ 1,126,003 | \$ 2,448,439 | \$ 2,562,445 |
| North American Business Solutions Division | 820,243 | 868,140 | 1,650,854 | 1,782,274 |
| International Division | 778,338 | 829,998 | 1,672,152 | 1,704,686 |
| Total | \$ 2,699,475 | \$ 2,824,141 | \$ 5,771,445 | \$ 6,049,405 |

| <i>(In thousands)</i> | Division Operating Profit (Loss) | | | |
|--|----------------------------------|-------------|------------|------------|
| | Second Quarter | | First Half | |
| | 2010 | 2009 | 2010 | 2009 |
| North American Retail Division | \$ 8,671 | \$ (13,091) | \$ 81,626 | \$ 68,253 |
| North American Business Solutions Division | 14,086 | 22,549 | 34,255 | 55,608 |
| International Division | 18,912 | 3,111 | 60,501 | 21,658 |
| Total | \$ 41,669 | \$ 12,569 | \$ 176,382 | \$ 145,519 |

A reconciliation of the measure of Division operating profit to consolidated earnings (loss) before income taxes is as follows:

| <i>(In thousands)</i> | Second Quarter | | First Half | |
|--|----------------|--------------|------------|--------------|
| | 2010 | 2009 | 2010 | 2009 |
| Total Division operating profit | \$ 41,669 | \$ 12,569 | \$ 176,382 | \$ 145,519 |
| Charges, as defined in Note D | | (35,020) | | (155,062) |
| Corporate general and administrative expenses (excluding Charges) | (69,265) | (75,478) | (148,475) | (148,843) |
| Interest income | 443 | 718 | 980 | 1,912 |
| Interest expense | (16,591) | (16,745) | (34,363) | (34,663) |
| Miscellaneous income (expense), net | 4,681 | 412 | 10,780 | (3,147) |
| Earnings (loss) before income taxes | \$ (39,063) | \$ (113,544) | \$ 5,304 | \$ (194,284) |

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Our Condensed Consolidated Balance Sheets as of June 26, 2010, December 26, 2009 and June 27, 2009 reflect a goodwill balance of approximately \$19.4 million, all of which is associated with our North American Business Solutions Division. The gross amount of goodwill and the amount of accumulated impairment losses as of June 26, 2010 are provided in the following table:

| <i>(Dollars in thousands)</i> | North American Retail Division | North American Business Solutions Division | International Division | Total |
|-------------------------------|---|---|-----------------------------------|------------------|
| Goodwill | \$ 1,842 | \$ 367,790 | \$ 863,134 | \$ 1,232,766 |
| Accumulated impairment losses | (1,842) | (348,359) | (863,134) | (1,213,335) |
| | \$ | \$ 19,431 | \$ | \$ 19,431 |

The balance and components of goodwill have remained constant since December 26, 2009.

Note H Employee Benefit Plans**Long-Term Incentive Plan**

In April 2010, shareholders approved an amendment to our Amended Long-Term Incentive Plan which allowed the company to implement a one-time voluntary stock option exchange for eligible employees. The fair value exchange was completed on June 8, 2010 with the tender of approximately 3.8 million shares of eligible options in exchange for approximately 1.4 million shares of newly-issued options. No additional compensation expense resulted from this exchange. The new options have an exercise price of \$5.13, which was the closing price of Office Depot, Inc. common stock on June 8, 2010, and generally will vest over three years.

Pension Disclosures

The components of net periodic pension cost (gain) for our foreign defined benefit plan are as follows:

| <i>(In millions)</i> | Second Quarter | | First Half | |
|----------------------------------|-----------------------|---------------|-------------------|---------------|
| | 2010 | 2009 | 2010 | 2009 |
| Service cost | \$ | \$ | \$ | \$ |
| Interest cost | 2.5 | 2.2 | 5.1 | 4.3 |
| Expected return on plan assets | (1.9) | (1.6) | (3.9) | (3.1) |
| Net periodic pension cost (gain) | \$ 0.6 | \$ 0.6 | \$ 1.2 | \$ 1.2 |

The pension plan was part of an entity acquired in 2003. The plan was curtailed and frozen in 2008 and no future service cost will be recognized. The purchase and sale agreement included a provision whereby the seller is required to pay to the company an amount of unfunded benefit obligation as measured based on certain 2008 data. The company is in arbitration to resolve the amount to be received from the seller. We currently cannot predict the outcome of this matter. The after-tax effect of any payment from the seller will be recognized as a credit to income when all associated uncertainties are resolved.

For the year-to-date 2010 period, we have contributed approximately \$2.5 million to our foreign pension plan. Every three years, the company meets with trustees to establish future funding targets with the intent of reducing the unfunded status of the plan. Based on the current funding arrangement, the company expects to contribute approximately \$5 million to the plan during 2010. However, this amount could change if a new agreement is reached with the trustees during 2010.

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Note I Income Taxes

During the second quarter of 2010, the company initiated a program to consolidate the beneficial economic rights related to certain worldwide intellectual property (IP). These rights were transferred through intercompany purchase and assignment agreements that generated gains which were eliminated in consolidation for financial reporting purposes. These transactions also resulted in the creation and reclassification of approximately \$37 million of prepaid tax accounts that will be recognized as tax expense in future periods to the extent the related IP is amortized or impaired for tax purposes. The prepaid tax is presented in other assets in the Condensed Consolidated Balance Sheet at June 26, 2010. In connection with these transactions, the company entered into an agreement with a foreign taxing jurisdictions which resulted in the reduction of existing uncertain tax positions by approximately \$15 million and the elimination of a corresponding amount of deferred tax assets that previously had been offset by these uncertain tax positions in our consolidated financial statements.

Our effective tax benefit rate was 75% for the second quarter of 2010 compared to a benefit rate of 27% for the same period in 2009. The 2010 effective tax benefit rate includes approximately \$13 million of discrete benefits from the release of a valuation allowance in Europe because of improved performance in that jurisdiction and a favorable settlement with certain taxing authorities. Also, the second quarter of 2010 rate includes the year to date impact of adjusting to our current estimate of our full year tax rate which resulted from fluctuations in the expected timing and amount of tax deductions of our book and tax temporary differences. Because the company has established a full valuation allowance on deferred taxes in the U. S., such changes in temporary differences result in tax rate volatility within interim periods.

During the third quarter of 2009, the company recognized valuation allowances totaling \$321.6 million, with \$279.1 million related to domestic deferred tax assets and \$42.5 million related to foreign deferred tax assets. The establishment of valuation allowances and development of projected annual effective tax rates requires significant judgment and is impacted by various estimates. Both positive and negative evidence, as well as the objectivity and verifiability of that evidence, is considered in determining the appropriateness of recording or maintaining valuation allowances on deferred tax assets. While the company recognized pretax earnings in the first half of 2010, sufficient positive evidence of deferred tax asset realizability to warrant removing the valuation allowances in the U.S. is not anticipated in the near term. However, in one foreign tax jurisdiction, sufficient positive evidence of deferred tax asset realizability arose during the second quarter of 2010, including attainment of cumulative positive earnings over the past three years and positive projections of operating performance, such that a valuation allowance of approximately \$10 million was released during the period.

We file a U.S. federal income tax return and other income tax returns in various states and foreign jurisdictions. With few exceptions, we are no longer subject to U.S. federal, state and local, or non-U.S. income tax examinations for years before 2000. Our U.S. federal filings for the years 2000 and 2002 through 2009 are under varying stages of routine examination, and it is reasonably possible that audits for some of these periods will be closed prior to the end of 2010. Additionally, the U.S. federal tax return for 2010 is under concurrent review. Significant international tax jurisdictions include the U.K., the Netherlands, France and Germany. Generally, we are subject to routine examination for years 2001 and forward in these jurisdictions. It is reasonably possible that certain of these audits will close within the next twelve months, which could result in a decrease of as much as \$106 million or an increase of as much as \$11 million to our accrued uncertain tax positions. Additionally, we anticipate that it is reasonably possible that new issues will be raised or resolved by tax authorities that may require changes to the balance of unrecognized tax benefits, however, an estimate of such changes cannot reasonably be made at this time.

Note J Fair Value Measurements

The company applies authoritative accounting guidance for fair value measurements of financial and nonfinancial assets and liabilities. This guidance defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The related rules provide the following hierarchy for measuring fair value:

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- Level 1: Quoted prices in active markets for identical assets or liabilities.
- Level 2: Observable marketbased inputs or unobservable inputs that are corroborated by market data.
- Level 3: Significant unobservable inputs that are not corroborated by market data. Generally, these fair value measures are model-based valuation techniques such as discounted cash flows or option pricing models using our own estimates and assumptions or those expected to be used by market participants.

Foreign currency contracts are valued at amounts receivable or payable to terminate the agreements at the reporting date and are based on observable market data for similar assets and liabilities. The carrying amounts of trade and other accounts receivable, trade and other accounts payable and other accrued expenses approximate fair value because of the short maturity of those instruments.

Fair value estimates may be required to measure certain assets and liabilities on a nonrecurring basis for asset impairments and exit cost valuations. No such impairments were recorded in the first half of 2010.

The following table summarizes the company's financial liabilities measured at fair value on a recurring basis:

| <i>(In thousands)</i> | June 26, 2010 | | | |
|----------------------------|---------------|---------|----------|---------|
| | Total | Level 1 | Level 2 | Level 3 |
| Liabilities: | | | | |
| Foreign exchange contracts | \$ 1,596 | \$ | \$ 1,596 | \$ |

The company records its senior notes payable at par value, adjusted for amortization of a fair value hedge which was cancelled in 2005. The fair value of the senior notes indicated in the following table was determined based on quoted market prices.

| <i>(In thousands)</i> | June 26, 2010 | | December 26, 2009 | | June 27, 2009 | |
|----------------------------|----------------|------------|-------------------|------------|----------------|------------|
| | Carrying Value | Fair Value | Carrying Value | Fair Value | Carrying Value | Fair Value |
| \$400 million senior notes | \$ 400,119 | \$ 387,480 | \$ 400,172 | \$ 345,966 | \$ 400,225 | \$ 320,000 |

Note K Derivative Instruments and Hedging Activity

As a global supplier of office products and services, we are exposed to risks associated with changes in foreign currency exchange rates, commodity prices, and interest rates. Our foreign operations are typically, but not exclusively, conducted in the currency of the local environment. We are exposed to the risk of foreign currency exchange rate changes when we make purchases, sell products, or arrange financings that are denominated in a currency different from the entity's functional currency. Depending on the settlement timeframe and other factors, we may enter into foreign currency derivative transactions to mitigate those risks. We may designate and account for such qualifying arrangements as hedges. Gains and losses on these cash flow hedging transactions are deferred in accumulated other comprehensive income (OCI) and recognized in earnings in the same period as the hedged item. Transactions that are not designated as cash flow hedges are marked to market at each period with changes in value included in earnings. Historically, we have not entered into transactions to hedge our net investment in foreign operations, but may in future periods.

We also are exposed to the risk of changing fuel prices from inbound and outbound transportation arrangements. Some transportation contracts may provide for specific identification of the fuel cost component such that the risk of fuel price changes may be offset by third-party contracts thereby allowing us to designate and qualify these offsetting contracts as cash flow hedges for accounting purposes. Deferred gains or losses associated with these arrangements would be recorded in OCI until such time as the hedged item impacts earnings. The structure of certain other transportation arrangements, however, precludes applying hedge accounting. In those circumstances, we may enter into derivative transactions to offset the risk of commodity price changes, and the value of the derivative contract is marked to market at each reporting period with changes recognized in earnings. As of June 26, 2010, the company had no fuel-related cash flow hedges outstanding.

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Interest rate changes on our obligations may result from external market factors, as well as changes in our credit rating. We manage our exposure to market risks at the corporate level. Interest rate-sensitive assets and liabilities are monitored and assessed for market risk. Currently, no interest-rate related derivative arrangements are in place. OCI includes the deferred gain from a hedge contract terminated in a prior period. This deferral is being amortized to interest expense through 2013.

Our risk management policies allow the use of specified financial instruments for hedging purposes only; speculation is not permitted.

The following tables provide information on our hedging and derivative positions and activity.

Fair Value of Derivative Instruments

| <i>(In thousands)</i> | Balance Sheet Location | Liability Derivatives | | Fair Value as of: | |
|--|---------------------------|-----------------------|----------------------|-------------------|-------|
| | | June 26, 2010 | December 26, 2009 | June 27, 2009 | |
| Derivatives designated as hedging instruments: | | | | | |
| Commodity contracts fuel | Other current liabilities | \$ | \$ | \$ | 3,072 |
| Foreign exchange contracts | Other current liabilities | 1,596 | 266 | | |
| Derivatives not designated as hedging instruments: | | | | | |
| Foreign exchange contracts | Other current liabilities | | | | 2,677 |
| Total liability derivatives | | \$ 1,596 | \$ 266 | \$ | 5,749 |

| Derivatives not designated as hedging instruments: <i>(In thousands)</i> | Location of gain/(loss) recognized in earnings | Amount of gain/(loss) recognized in earnings | |
|--|---|---|-------------------------------------|
| | | Second Quarter 2009 | First Half 2009 |
| | | Foreign exchange contracts | Miscellaneous income (expense), net |
| Total | | \$ (5,770) | \$ (10,325) |

| Derivatives designated as hedging instruments: <i>(In thousands)</i> | Amount of gain/(loss) recognized in OCI | | Location of gain/(loss) reclassified from OCI into earnings | Amount of gain/(loss) reclassified from OCI into earnings | |
|--|--|---------------|---|---|-----------------------|
| | Second Quarter | First Half | | Second Quarter 2010 | First Half 2010 |
| | | | | | |

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| | 2010 | 2010 | | | |
|----------------------------|------------|------------|--|----------|------------|
| Foreign exchange contracts | \$ (2,252) | \$ (2,870) | Cost of goods sold and occupancy costs | \$ (818) | \$ (1,455) |
| Total 2010 | \$ (2,252) | \$ (2,870) | | \$ (818) | \$ (1,455) |

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| Derivatives designated as hedging instruments: | Amount of gain/(loss) recognized in OCI | | Location of gain/(loss) reclassified from OCI into earnings | Amount of gain/(loss) reclassified from OCI into earnings | |
|---|--|--------------------|--|---|-----------------------|
| | Second Quarter 2009 | First Half 2009 | | Second Quarter 2009 | First Half 2009 |
| | (In thousands) | | | | |
| Commodity contracts fuel hedges | \$ 1,330 | \$ 2,919 | Cost of goods sold and occupancy costs & Store and warehouse operating and selling expenses* | \$ (2,430) | \$ (5,115) |
| Total 2009 | \$ 1,330 | \$ 2,919 | | \$ (2,430) | \$ (5,115) |

* Approximately 60% of the losses for the second quarter and first half of 2009 are reflected in cost of goods sold and occupancy costs. The remaining 40% of the losses are reflected in store and warehouse operating and selling expenses.

The existing hedge contracts are highly effective and the ineffective portion is considered immaterial. The foreign exchange contracts extend through December 2010. Losses currently deferred in OCI are expected to be recognized in earnings within the next twelve months. As of June 26, 2010, there were no arrangements requiring collateral. However, we may be required to provide collateral on certain arrangements in the future. The fair values of our foreign currency contracts and fuel contracts are the amounts receivable or payable to terminate the agreements at the reporting date, taking into account current exchange rates. The values are based on market-based inputs or unobservable inputs that are corroborated by market data.

Note L Investment in Unconsolidated Joint Venture

Since 1994, we have participated in a joint venture in Mexico, Office Depot de Mexico. Because we participate equally in this business with a partner, we account for this investment using the equity method. Our proportionate share of Office Depot de Mexico's net income or loss is presented in miscellaneous income, net in the Condensed Consolidated Statements of Operations.

The following tables provide summarized unaudited information from the balance sheets and statements of earnings for Office Depot de Mexico:

| (In thousands) | June 26, 2010 | December 26, 2009 | June 27, 2009 |
|-------------------------|------------------|----------------------|------------------|
| Current assets | \$ 260,069 | \$ 219,030 | \$ 208,701 |
| Non-current assets | 269,364 | 260,074 | 246,014 |
| Current liabilities | 157,954 | 141,944 | 160,786 |
| Non-current liabilities | 2,285 | | |

| (In thousands) | Second Quarter 2010 | | First Half 2009 | |
|----------------|------------------------|------------|--------------------|------------|
| | 2009 | 2009 | 2010 | 2009 |
| Sales | \$ 208,338 | \$ 185,693 | \$ 427,755 | \$ 380,092 |
| Gross profit | 60,988 | 54,667 | 123,384 | 108,998 |

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| | | | | |
|------------|--------|--------|--------|--------|
| Net income | 10,671 | 11,725 | 24,639 | 24,173 |
|------------|--------|--------|--------|--------|

During the first quarter of 2009, we received a \$13.9 million dividend from this venture.

Table of Contents**Note M Commitments and Contingencies**

We are involved in litigation arising in the normal course of our business. While, from time to time, claims are asserted that make demands for a large sum of money (including, from time to time, actions which are asserted to be maintainable as class action suits), we do not believe that contingent liabilities related to these matters, either individually or in the aggregate, will materially affect our financial position, results of our operations or cash flows.

As previously disclosed, the company reached a proposed settlement with the staff of the U.S. Securities and Exchange Commission (SEC) to resolve the previously disclosed SEC inquiry that commenced in July of 2007 and the formal investigation disclosed in January of 2008 with respect to contacts and communications with financial analysts, inventory receipt and reserves, timing of vendor payments, certain intercompany loans, certain payments to foreign officials, inventory obsolescence and timing and recognition of vendor program funds. The company and its officers and employees have cooperated with the SEC staff in this investigation. The SEC staff intends to recommend to the SEC a proposed settlement with respect to the company which would conclude for the company all matters arising from the SEC investigation. Under the proposed settlement, the company, without admitting or denying liability, will agree to pay a civil penalty and to consent to a cease and desist order from committing or causing violations of Sections 13(a) and 13(b) of the Securities Exchange Act of 1934 (and related rules) which require the maintenance of accurate books and records and internal controls, and Regulation FD. Regulation FD is a rule regarding communication with analysts and investors. The proposed settlement is contingent on approval by the SEC Commissioners. There can be no assurance that the SEC Commissioners will approve the staff's recommendation. The company has also been informed that the company's Chief Executive Officer and the company's former Chief Financial Officer have also reached proposed settlements with the SEC staff related to Regulation FD, which, if approved by the SEC Commissioners, would also conclude for the CEO all matters arising from the SEC investigation. Under those proposed settlements, without admitting or denying liability, each will agree to remain in compliance with Regulation FD and related securities laws and undertake a civil penalty. The proposed settlement would not affect Mr. Odland's position as Chairman and CEO of the company.

On January 14, 2010, the federal court in the Southern District of Florida dismissed the Second Consolidated Amended Complaint filed by the New Mexico Educational Retirement Board, lead plaintiff in the Consolidated Lawsuit (defined below), with prejudice. On February 9, 2010, the lead plaintiff filed a notice to appeal this decision, and that appeal remains pending. As background, in early November 2007, two putative class action lawsuits were filed against the company and certain of its executive officers alleging violations of the Securities Exchange Act of 1934. The allegations made in these lawsuits primarily related to the accounting for vendor program funds. Each of the foregoing lawsuits was filed in the Southern District of Florida and captioned as follows: (1) Nichols v. Office Depot, Inc., Steve Odland and Patricia McKay filed on November 6, 2007 and (2) Sheet Metal Worker Local 28 Pension Fund v. Office Depot, Inc., Steve Odland and Patricia McKay filed on November 5, 2007. On March 21, 2008, the court in the Southern District of Florida entered an Order consolidating the class action lawsuits (the Consolidated Lawsuit). Lead plaintiff in the Consolidated Lawsuit, the New Mexico Educational Retirement Board, filed its Consolidated Amended Complaint on July 2, 2008, and its Second Consolidated Amended Complaint on April 20, 2009.

In addition, in the ordinary course of business, our sales to and transactions with government customers may be subject to audits and review by governmental authorities and regulatory agencies. Many of these audits and reviews are resolved without incident; however, we have had an increasing number of claims and inquiries by certain governmental agencies into contract pricing, and additional inquiries may follow. While these claims may assert large demands, we do not believe that contingent liabilities related to these matters, either individually or in the aggregate, will materially affect our financial position, results of our operations or cash flows.

Note N Subsequent Events

Since 1996, we have been selling products through a third-party, non-profit government purchasing cooperative available to local and state government agencies, schools and non-profit organizations nationwide. That cooperative offers products through competitively solicited contracts with lead governmental agencies. The lead government agency contract for office supplies, which has been in place since 2006 and for which we are the provider, expires on January 1, 2011 and the agency has solicited proposals for a new office supplies contract (the RFP). In July 2010, the company decided not to submit a proposal. The company believes that the RFP contains terms that are problematic and could lead to an operating loss with respect to this business. We will continue our relationship with the cooperative through the expiration of our current agreement and through our national lead agency contracts for technology and school supplies. We intend to work aggressively to retain our customers related to this particular business and grow the business directly and through new cooperative agreements.

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

GENERAL

Office Depot, Inc., together with our subsidiaries, is a global supplier of office products and services. We sell to consumers and businesses of all sizes through our three segments (or Divisions): North American Retail Division, North American Business Solutions Division, and International Division.

Management's Discussion and Analysis of Financial Condition and Results of Operations (MD&A) is intended to provide information to assist in better understanding and evaluating our financial condition and results of operations. We recommend that you read this MD&A in conjunction with our condensed consolidated financial statements and the notes to those statements included in Item 1 of this Quarterly Report on Form 10-Q, as well as our 2009 Annual Report on Form 10-K (the 2009 Form 10-K), filed with the U.S. Securities and Exchange Commission (the SEC).

This MD&A contains significant amounts of forward-looking information. Without limitation, when we use the words believe, estimate, plan, expect, intend, anticipate, continue, may, project, probably, should, could, will and similar expressions in this Quarterly Report, we are identifying forward-looking statements (as such term is defined in the Private Securities Litigation Reform Act of 1995). Our discussion of Risk Factors, found in Item 1A of this Form 10-Q and our 2009 Form 10-K, and Forward-Looking Statements, found immediately following the MD&A in our 2009 Form 10-K, apply to these forward-looking statements.

RESULTS OF OPERATIONS

OVERVIEW

A summary of factors important to understanding the results for the second quarter of 2010 is provided below and further discussed in the narrative that follows this overview.

Sales in the second quarter of 2010 decreased 4% compared to the second quarter of 2009. Sales in North America were down 4%, and North American Retail Division comparable store sales decreased 1% for the quarter. International sales decreased 6% in U.S. dollars and 3% in local currencies.

Total operating expenses were down approximately 8% compared to the second quarter of 2009. Operating expenses for the second quarter of 2009 included \$35 million of charges related to our previously announced strategic reviews (the Charges). We did not recognize new Charges under these programs in the second quarter or first half of 2010.

Our effective tax benefit rate for the second quarter of 2010 was 75%, reflecting discrete impacts of the release of a valuation allowance and certain uncertain tax position accruals, as well as our adjustment the full year tax rate based on the anticipated timing of tax deductions for the year. The valuation allowance established in the U.S. during prior quarters has introduced the potential for significant volatility to our interim period effective tax rate.

We reported a net loss available to common shareholders of \$19 million for the second quarter of 2010 compared to a loss available to common shareholders of \$83 million in the same quarter of the prior year. We reported a loss per share of \$0.07 in the second quarter of 2010, compared to a loss per share of \$0.31 in the second quarter of 2009. In the second quarter of 2009, after-tax Charges negatively impacted earnings per share by \$0.09.

Table of Contents**DIVISION RESULTS**North American Retail Division

| <i>(Dollars in millions)</i> | Second Quarter | | First Half | |
|----------------------------------|-----------------------|-------------|-------------------|-------------|
| | 2010 | 2009 | 2010 | 2009 |
| Sales | \$ 1,100.9 | \$ 1,126.0 | \$ 2,448.4 | \$ 2,562.4 |
| % change | (2)% | (21)% | (4)% | (19)% |
| Division operating profit (loss) | \$ 8.7 | \$ (13.1) | \$ 81.6 | \$ 68.3 |
| % of sales | 0.8% | (1.2)% | 3.3% | 2.7% |

Second quarter sales in the North American Retail Division were \$1.1 billion, down 2% from the prior year. Comparable store sales in the 1,132 stores in the U.S. and Canada that have been open for more than one year decreased 1% for the quarter. The second quarter 2010 customer transaction counts were down slightly compared to the same period last year and continued to drive the overall comparable sales decline. Our average order value increased compared to the prior year for the second consecutive quarter. Sales in our supplies and technology categories were relatively consistent with the first quarter and the furniture category maintained positive comparable sales, though lower sequentially from the first quarter. Geographically, our best performing sales markets were the Midwest and the Northeast, both of which achieved positive comparable store sales. Sales in California improved slightly, though that region is expected to face continued economic challenges.

The North American Retail Division reported operating profit of approximately \$9 million in the second quarter of 2010, compared to a loss of \$13 million in the same period of 2009. This measure of operating performance is consistent with the internal reporting of results used to manage the business and allocate resources and does not include Charges incurred in the second quarter and first half of 2009. Please see Charges discussion in the Corporate and Other section below.

The increase in Division operating profit for the second quarter of 2010 was driven by favorable product margins from our ongoing product line reviews and increased direct import penetration, as well as the absence of a \$5 million charge recognized in the second quarter of 2009 to reflect updated assumptions on subleases of closed stores. The factors discussed above for the second quarter also address the first half of 2010 compared to the same period in 2009. Additionally, results for the first quarter of 2010 reflect the closure of 120 stores during 2009 as part of the strategic review initiated during the fourth quarter of 2008, as well as increased advertising expenses, partially offset by positive inventory shrinkage impacts compared to the prior year.

At the end of the second quarter of 2010, Office Depot operated 1,152 office products stores throughout the U.S. and Canada. We opened seven stores and closed four stores during the period.

North American Business Solutions Division

| <i>(Dollars in millions)</i> | Second Quarter | | First Half | |
|------------------------------|-----------------------|-------------|-------------------|-------------|
| | 2010 | 2009 | 2010 | 2009 |
| Sales | \$ 820.2 | \$ 868.1 | \$ 1,650.9 | \$ 1,782.3 |
| % change | (6)% | (18)% | (7)% | (18)% |
| Division operating profit | \$ 14.1 | \$ 22.5 | \$ 34.3 | \$ 55.6 |
| % of sales | 1.7% | 2.6% | 2.1% | 3.1% |

Second quarter sales in the North American Business Solutions Division were \$820 million, down 6% compared to the second quarter of 2009. Average order value for the second quarter of 2010 was relatively flat compared to the same period in the prior year. The decline in Division sales for both the second quarter and first half of 2010 was driven by lower transaction counts as customers continued to exercise caution on discretionary spending for office supplies. The comparison of Division sales for the second quarter of 2010 and 2009 was also negatively impacted by restructuring

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certain non-core businesses late in 2009. Sales in the direct channel were relatively flat compared to the same period in 2009 with many product categories showing positive growth. The contract channel sales continued to decline, reflecting challenges in the governmental sector and lower sales to small- to medium-sized businesses. Sales in our Copy and Print Depot and the cleaning and break room supply categories performed well in both the second quarter and first half of 2010.

The North American Business Solutions Division reported operating profit of approximately \$14 million in the second quarter of 2010, compared to \$23 million in the same period of the prior year. This decrease reflects the unfavorable impact our sales volume decline had on gross margin and operating expenses (the flow through impact). Additionally, the second quarter of 2009 included benefits from lower inventory shrinkage and customer rebates. The factors discussed for the second quarter results are largely the same factors impacting the first half of 2010 compared to 2009.

Since 1996, we have been selling products through a third-party, non-profit government purchasing cooperative available to local and state government agencies, schools and non-profit organizations nationwide. That cooperative offers products through competitively solicited contracts with lead governmental agencies. The lead government agency contract for office supplies, which has been in place since 2006 and for which we are the provider, expires on January 1, 2011 and the agency has solicited proposals for a new office supplies contract (the RFP). In July 2010, the company decided not to submit a proposal. The company believes that the RFP contains terms that are problematic and could lead to an operating loss with respect to this business. Currently, operating profit for this business is in the low single digits as a percentage of projected annual sales of approximately \$515 million. We will continue our relationship with the cooperative through the expiration of our current agreement and through our national lead agency contracts for technology and school supplies. We intend to work aggressively to retain our customers related to this particular business and grow the business directly and through new cooperative agreements.

International Division

| <i>(Dollars in millions)</i> | Second Quarter | | First Half | |
|----------------------------------|-----------------------|-------------|-------------------|-------------|
| | 2010 | 2009 | 2010 | 2009 |
| Sales | \$ 778.3 | \$ 830.0 | \$ 1,672.2 | \$ 1,704.7 |
| % change | (6)% | (25)% | (2)% | (24)% |
| % change in local currency sales | (3)% | (12)% | (4)% | (10)% |
| Division operating profit | \$ 18.9 | \$ 3.1 | \$ 60.5 | \$ 21.7 |
| % of sales | 2.4% | 0.4% | 3.6% | 1.3% |

The International Division reported second quarter sales of \$778 million, reflecting a decrease of 6% in U.S. dollars and 3% in local currencies compared to the second quarter of 2009. The closing of retail stores in Japan during 2009 accounted for approximately 1% of the local currency sales decline. The second quarter sales decline rate varied geographically across the Division. Local currency sales in the U.K. and Germany improved sequentially from the first quarter, and increased in the Asia region, after considering the Japan retail store closures last year. The contract channel sales in local currency increased slightly compared to the second quarter of 2009. However, our public sector business has been negatively impacted by the actions taken by governments across Europe in response to the recent debt crisis and budgetary constraints. Second quarter sales in the direct channel were lower than the same period in 2009, though the rate of decline has improved compare to prior quarters. The retail channel reported positive sales growth, after considering the Japan retail store closures last year.

The International Division reported operating profit of approximately \$19 million in the second quarter of 2010, compared to \$3 million in the same period of 2009. This measure of operating performance is consistent with the internal reporting of results used to manage the business and allocate resources and does not include Charges incurred in the second quarter and first half of 2009. Please see Charges discussion in the Corporate and Other section below.

The increase in Division operating profit for the second quarter of 2010 resulted from a number of factors including better pricing management, reduced distribution costs and general and administrative expenses, as well as our exit from the retail business in Japan last year. These positive factors more than offset the flow through impact of lower sales. The factors discussed for the second quarter results are largely the same factors impacting the first half of 2010 compared to 2009. The change in exchange rates negatively impacted operating profit in U.S. dollars by approximately \$2 million for the second quarter of 2010 and had a positive impact of approximately \$1 million for the first half of 2010, compared to the same periods in 2009.

Table of Contents**CORPORATE AND OTHER****Charges**

During prior years, we performed internal reviews of assets and processes with the goal of positioning the company to deal with the degradation in the global economy and to benefit from its eventual improvement. The results of those reviews led to decisions to close stores, exit certain businesses and write off certain assets that were not seen as providing future benefit. These decisions resulted in material charges that were recognized during the fourth quarter of 2008 and fiscal year 2009. Our measurement of Division operating profit excludes the Charges because they are evaluated internally at the corporate level.

As of the end of 2009, we had substantially completed all activities falling under our strategic reviews. Although we did not recognize new Charges under these programs in the second quarter and first half of 2010, positive and negative adjustments to previously accrued amounts as well as accretion on discounted long-term accruals such as lease obligations impacted our results in the period. Amortizations, settlements, and adjustments to related existing accruals are included in store and warehouse operating and selling expenses and recognized at the corporate level.

During the second quarter and first half of 2009, we recognized approximately \$35 million and \$155 million, respectively, of Charges associated with these activities as the previously-identified plans were implemented and the related accounting recognition criteria were met. For the second quarter Charges, approximately \$30 million is included in store and warehouse operating and selling expenses and \$5 million is included in general and administrative expenses on our Condensed Consolidated Statement of Operations. For the first half Charges, approximately \$126 million is included in store and warehouse operating and selling expenses and \$19 million in general and administrative expenses, and \$10 million is included in cost of goods sold and occupancy costs.

General and Administrative Expenses

The portion of General and Administrative (G&A) expenses considered directly or closely related to unit activity is included in the measurement of Division operating profit. Other companies may charge more or less G&A expenses and other costs to their segments, and our results therefore may not be comparable to similarly titled measures used by other entities. Our measure of Division operating profit should not be considered as an alternative to operating income or net earnings determined in accordance with accounting principles generally accepted in the United States of America.

Total G&A decreased from \$170 million in the second quarter of 2009 to \$152 million in the second quarter of 2010. A breakdown of G&A between the portion included in Division results and the portion considered corporate expenses is provided in the following table:

| <i>(In millions)</i> | Second Quarter | | First Half | |
|----------------------|-----------------------|-----------------|-------------------|-----------------|
| | 2010 | 2009 | 2010 | 2009 |
| Division G&A | \$ 83.2 | \$ 89.8 | \$ 171.2 | \$ 179.0 |
| Corporate G&A | 68.7 | 80.6 | 148.9 | 167.8 |
| Total G&A | \$ 151.9 | \$ 170.4 | \$ 320.1 | \$ 346.8 |

Corporate G&A included Charges of \$5 million and \$19 million in the second quarter and first half of 2009, respectively, and none in 2010. After considering the impact of Charges recognized in the 2009 periods, corporate G&A decreased by approximately \$7 million during the second quarter of 2010 compared to the same period of 2009. This decrease primarily reflects an adjustment to variable-based pay arrangements that are influenced, in part, from changes in foreign currency exchange rates, partially offset by increased depreciation expense related to the company's implementation of a new enterprise software system which was placed in service at the beginning of the third quarter of 2009.

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Other income (expense)

The increase in net miscellaneous income (expense) in the second quarter and first half of 2010 primarily reflects lower foreign currency losses in 2010 compared to the same periods of 2009.

Income Taxes

Our effective tax benefit rate was 75% for the second quarter of 2010 compared to a benefit rate of 27% for the same period in 2009. The 2010 effective tax benefit rate includes approximately \$13 million of discrete benefits from the release of a valuation allowance in Europe because of improved performance in that jurisdiction and a favorable settlement with certain taxing authorities. Also, the second quarter of 2010 rate includes the year to date impact of adjusting to our current estimate of our full year tax rate which resulted from fluctuations in the expected timing and amount of tax deductions of our book and tax temporary differences. Because the company has established a full valuation allowance on deferred taxes in the U. S., such changes in temporary differences result in tax rate volatility within interim periods. We currently anticipate our annual effective tax rate to be a benefit of approximately 13%; however, we have experienced volatility in both the first and second quarters of 2010 and such volatility could continue based on the extent and mix of income, as well as the anticipated recognition of temporary book to tax differences.

The valuation allowances were established in 2009 on deferred tax assets in both the U.S. and certain foreign tax jurisdictions. While the company recognized pretax earnings in the first half of 2010, and is optimistic about future performance, sufficient positive evidence of deferred tax asset realizability to warrant removing the valuation allowances in the U.S. is not anticipated in the near term. The company is exploring the feasibility of potential international tax restructuring activities, that along with continued positive operating performance in the relevant jurisdictions, may allow removal of certain additional foreign valuation allowances sooner than in the U.S. This may occur in the near term, possibly within the next twelve months. It is possible that the company may not be able to implement its tax planning strategy. Until all significant valuation allowances are removed, the company likely will experience volatility in our effective tax rate. In addition to the volatility from limited deferred tax accounting, increases or decreases in uncertain tax provisions following completion of examinations of open tax years may have significant impacts on the effective tax rate. Completion of certain examinations are anticipated during 2010.

During the second quarter of 2010, the company initiated a program to consolidate the beneficial economic rights related to certain worldwide intellectual property (IP). These rights were transferred through intercompany purchase and assignment agreements that generated gains which were eliminated in consolidation for financial reporting purposes. These transactions also resulted in the creation and reclassification of approximately \$37 million of prepaid tax accounts that will be recognized as tax expense in future periods to the extent the related IP is amortized or impaired for tax purposes. The prepaid tax is presented in other assets in the Condensed Consolidated Balance Sheet at June 26, 2010. In connection with these transactions, the company entered into an agreement with certain foreign taxing jurisdictions which resulted in the reduction of existing uncertain tax positions by approximately \$15 million and the elimination of a corresponding amount of deferred tax assets that previously had been offset by these uncertain tax positions in our consolidated financial statements. Additional IP transfers are likely to be initiated later in 2010 in furtherance of this program.

LIQUIDITY AND CAPITAL RESOURCES

At June 26, 2010, we had approximately \$578 million in cash and equivalents and another \$680 million available under our asset based credit facility (the Facility) based on the June borrowing base certificate. We consider our resources adequate to satisfy our cash needs at least over the next twelve months. We anticipate that market conditions will continue to be challenging through 2010, and in response, we are focused on maximizing cash flow.

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At June 26, 2010, we were not drawn on the Facility. There were letters of credit outstanding under the Facility totaling approximately \$146 million. An additional \$0.5 million of letters of credit were outstanding under separate agreements. The company did not borrow under the Facility during the first half of 2010. During the second quarter of 2010, the company cancelled the accounts receivable factoring arrangement established during 2009 in Europe without having sold any receivables. The company was in compliance with all applicable financial covenants at June 26, 2010.

Dividends on the company's redeemable preferred stock are payable quarterly, and will be paid in-kind or, in cash, only to the extent that the company has funds legally available for such payment and a cash dividend is declared by the company's board of directors. On March 26, 2010, the company executed a second amendment to the Facility allowing, among other things, the company to pay cash dividends on preferred stock and make share repurchases, in an aggregate amount of \$50 million per fiscal year subject to the satisfaction of certain liquidity requirements.

During the first half of 2010, cash provided by operating activities totaled \$32 million compared to \$106 million during the same period last year. The first half of 2009 net loss included significant non-cash Charges that increased working capital accruals for severance and lease obligations. The working capital and other use of cash in 2010 reflects cash payments of approximately \$49 million related to these prior restructuring efforts, as well payments on other accruals. The source of cash in the 2009 period was driven by our collection of accounts receivable balances and controlling our inventory levels. Additionally, the first half of 2009 includes a \$14 million dividend received from our joint venture in Mexico, Office Depot de Mexico. Working capital is influenced by a number of factors including the flow of goods, credit terms, timing of promotions, vendor production planning, new product introductions and working capital management. For our accounting policy on cash management, see Note A of the Notes to Condensed Consolidated Financial Statements.

Cash used in investing activities was \$76 million in the first half of 2010, compared to a source of cash of \$101 million in the same period last year. The use of cash in 2010 reflects capital expenditures of approximately \$83 million and an \$11 million payment to complete a prior acquisition, partially offset by approximately \$17 million of proceeds from the disposition of assets. The source of cash in 2009 reflects \$147 million of proceeds from several sale and sale-leaseback transactions related to the strategic review and our efforts to enhance our liquidity and the release of \$6 million of cash that had been held in a restricted account at the end of 2008. These sources were offset by capital expenditures of approximately \$54 million for the first half of 2009.

Cash used in financing activities was approximately \$15 million for the first half of 2010, compared to a source of cash of \$188 million in the same period last year. During the first half of 2010, we paid a cash dividend on our convertible preferred stock of approximately \$9 million. An additional approximately \$9 million was accrued during the second quarter and subsequently paid on July 1, 2010. Other outflows during the first half of 2010 included fees related to the amendment of our asset based credit facility and net payments on borrowings, including capital leases, partially offset by inflows from employee share-based transactions and related tax benefits. The source of cash in the first half of 2009 resulted from our issuance of redeemable preferred stock during the second quarter. Uses of cash during the first half of 2009 included \$139 million in payments made on our asset based credit facility and \$31 million in capital lease payments. Also, during the first half of 2009, we incurred approximately \$19 million in debt as a result of a land sale and leaseback that was treated as a financing transaction as well as approximately \$12 million of other short-term borrowings.

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CRITICAL ACCOUNTING POLICIES

Our condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America. Preparation of these statements requires management to make judgments and estimates. Some accounting policies have a significant impact on amounts reported in these financial statements. A summary of significant accounting policies and a description of accounting policies that are considered critical may be found in our 2009 Form 10-K, filed on February 23, 2010, in Note A of the Notes to the Consolidated Financial Statements and the Critical Accounting Policies section of the Management's Discussion and Analysis of Financial Condition and Results of Operations.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Interest Rate Risks

At June 26, 2010, there had not been a material change in the interest rate risk information disclosed in the Market Sensitive Risks and Positions subsection of the Management's Discussion and Analysis of Financial Condition and Results of Operations set forth in Item 7 of our 2009 Form 10-K.

Foreign Exchange Rate Risks

At June 26, 2010, there had not been a material change in any of the foreign exchange risk information disclosed in the Market Sensitive Risks and Positions subsection of the Management's Discussion and Analysis of Financial Condition and Results of Operations set forth in Item 7 of our 2009 Form 10-K.

Item 4. Controls and Procedures

We maintain controls and other procedures that are designed to ensure that information required to be disclosed by us in the reports that we file or submit under the Securities Exchange Act of 1934, as amended (the Exchange Act) is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be in this report is accumulated and communicated to its management, including its principal executive officer and principal financial officer, as appropriate, to allow timely decisions regarding required disclosure. Our management recognizes that any controls and procedures, no matter how well designed and operated, can only provide reasonable assurance of achieving their objectives and management necessarily applies its judgment in evaluating the possible controls and procedures.

Based on management's evaluation, which included the participation of the company's Chief Executive Officer (CEO), and Chief Financial Officer (CFO), as of June 26, 2010, the company's CEO and CFO concluded that the company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the Act), were effective to provide reasonable assurance that information required to be disclosed by the company in reports that the company files or submits under the Act is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms and that such information is accumulated and communicated to the company's management, including the CEO and CFO, to allow timely decisions regarding required disclosures.

Changes in Internal Control over Financial Reporting

There has been no change in the company's internal control over financial reporting that occurred during the company's most recent second quarter that has materially affected, or is reasonably likely to materially affect, the company's internal control over financial reporting.

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PART II. OTHER INFORMATION

Item 1. Legal Proceedings

We are involved in litigation arising in the normal course of our business. While, from time to time, claims are asserted that make demands for a large sum of money (including, from time to time, actions which are asserted to be maintainable as class action suits), we do not believe that contingent liabilities related to these matters, either individually or in the aggregate, will materially affect our financial position, results of our operations or cash flows.

As previously disclosed, the company reached a proposed settlement with the staff of the U.S. Securities and Exchange Commission (SEC) to resolve the previously disclosed SEC inquiry that commenced in July of 2007 and the formal investigation disclosed in January of 2008 with respect to contacts and communications with financial analysts, inventory receipt and reserves, timing of vendor payments, certain intercompany loans, certain payments to foreign officials, inventory obsolescence and timing and recognition of vendor program funds. The company and its officers and employees have cooperated with the SEC staff in this investigation. The SEC staff intends to recommend to the SEC a proposed settlement with respect to the company which would conclude for the company all matters arising from the SEC investigation. Under the proposed settlement, the company, without admitting or denying liability, will agree to pay a civil penalty and to consent to a cease and desist order from committing or causing violations of Sections 13(a) and 13(b) of the Securities Exchange Act of 1934 (and related rules) which require the maintenance of accurate books and records and internal controls, and Regulation FD. Regulation FD is a rule regarding communication with analysts and investors. The proposed settlement is contingent on approval by the SEC Commissioners. There can be no assurance that the SEC Commissioners will approve the staff's recommendation. The company has also been informed that the company's Chief Executive Officer and the company's former Chief Financial Officer have also reached proposed settlements with the SEC staff related to Regulation FD, which, if approved by the SEC Commissioners, would also conclude for the CEO all matters arising from the SEC investigation. Under those proposed settlements, without admitting or denying liability, each will agree to remain in compliance with Regulation FD and related securities laws and undertake a civil penalty. The proposed settlement would not affect Mr.Odland's position as Chairman and CEO of the company.

On January 14, 2010, the federal court in the Southern District of Florida dismissed the Second Consolidated Amended Complaint filed by the New Mexico Educational Retirement Board, lead plaintiff in the Consolidated Lawsuit (defined below), with prejudice. On February 9, 2010, the lead plaintiff filed a notice to appeal this decision, and that appeal remains pending. As background, in early November 2007, two putative class action lawsuits were filed against the company and certain of its executive officers alleging violations of the Securities Exchange Act of 1934. The allegations made in these lawsuits primarily related to the accounting for vendor program funds. Each of the foregoing lawsuits was filed in the Southern District of Florida and captioned as follows: (1) Nichols v. Office Depot, Inc., Steve Odland and Patricia McKay filed on November 6, 2007 and (2) Sheet Metal Worker Local 28 Pension Fund v. Office Depot, Inc., Steve Odland and Patricia McKay filed on November 5, 2007. On March 21, 2008, the court in the Southern District of Florida entered an Order consolidating the class action lawsuits (the Consolidated Lawsuit). Lead plaintiff in the Consolidated Lawsuit, the New Mexico Educational Retirement Board, filed its Consolidated Amended Complaint on July 2, 2008, and its Second Consolidated Amended Complaint on April 20, 2009.

In addition, in the ordinary course of business, our sales to and transactions with government customers may be subject to audits and review by governmental authorities and regulatory agencies. Many of these audits and reviews are resolved without incident; however, we have had an increasing number of claims and inquiries by certain governmental agencies into contract pricing, and additional inquiries may follow. While these claims may assert large demands, we do not believe that contingent liabilities related to these matters, either individually or in the aggregate, will materially affect our financial position, results of our operations or cash flows.

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Item 1A. Risk Factors.

With the exception of a change to the following previously disclosed risk factor, there have been no material changes in our risk factors from those disclosed in Part 1, Item 1A of our Quarterly Report on Form 10-Q for the quarterly period ended March 27, 2010.

Government Contracts One of our largest U.S. customers is a buying cooperative. Thousands of public agencies participate in this group, including various state and local governments, government agencies and non-profit organizations. Collectively, sales to these various organizations in 2009 represented approximately 5% of total company sales. Our relationship with this customer group is subject to uncertain future funding levels and applicable procurement laws and requires restrictive contract terms; any of these factors could curtail current or future business. This customer group offers products through competitively solicited contracts with lead government agencies. The lead government agency contract for office supplies, which has been in place since 2006 and for which we are the provider, expires on January 1, 2011. In July 2010, we decided not to submit a proposal in response to the current request for proposal regarding this lead agency contract. We believe the request for proposal contains terms that are problematic and could lead to an operating loss with respect to this business. We intend to work aggressively to retain our customers related to this particular business and grow the business directly and through new cooperative agreements. Contracting with government agencies is highly competitive and can be expensive and time-consuming, often requiring that we incur significant upfront time and expense without any assurance that we will win a contract. Our ability to compete successfully for and retain business with the federal and various state and local governments is highly dependent on cost-effective performance. Our government business is also sensitive to changes in national and international priorities and U.S., state and local government budgets.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

In March 2010, the company executed a second amendment to its asset based credit facility, allowing, among other things, the company to pay cash dividends on preferred stock and make share repurchases, in an aggregate amount of \$50 million per fiscal year subject to the satisfaction of certain liquidity requirements. Also, so long as investors in the redeemable preferred stock own at least 10% of the common stock voting rights, on an as-converted basis, the affirmative vote of a majority of the shares of preferred stock then outstanding and entitled to vote is required for the declaration or payment of a dividend on common stock. The company has never declared or paid cash dividends on its common stock.

Item 6. Exhibits

Exhibits

| | |
|---------|---|
| 31.1 | Rule 13a-14(a)/15d-14(a) Certification of CEO |
| 31.2 | Rule 13a-14(a)/15d-14(a) Certification of CFO |
| 32 | Section 1350 Certification |
| 101.INS | XBRL Instance Document |
| 101.SCH | XBRL Taxonomy Extension Schemat |
| 101.CAL | XBRL Taxonomy Extension Calculation Linkbase |
| 101.LAB | XBRL Taxonomy Extension Label Linkbase |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase |

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

OFFICE DEPOT, INC.

(Registrant)

Date: July 27, 2010

By: /s/ Steve Odland
Steve Odland
Chief Executive Officer and
Chairman, Board of Directors
(Principal Executive Officer)

Date: July 27, 2010

By: /s/ Michael D. Newman
Michael D. Newman
Executive Vice President and
Chief Financial Officer
(Principal Financial Officer)

Date: July 27, 2010

By: /s/ Mark E. Hutchens
Mark E. Hutchens
Senior Vice President
and Controller
(Principal Accounting Officer)