

OFFICE DEPOT INC  
Form 10-Q  
August 04, 2015  
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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 27, 2015

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)

59-2661354  
(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  Accelerated filer

Non-accelerated filer  (Do not check if a smaller reporting company) 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 27, 2015, there were 548,138,078 outstanding shares of Office Depot, Inc. Common Stock, \$0.01 par value.

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	<b>13 Weeks Ended</b>		<b>26 Weeks Ended</b>	
	<b>June 27, 2015</b>	<b>June 28, 2014</b>	<b>June 27, 2015</b>	<b>June 28, 2014</b>
Sales	\$ 3,440	\$ 3,841	\$ 7,317	\$ 8,194
Cost of goods sold and occupancy costs	2,626	2,958	5,566	6,296
Gross profit	814	883	1,751	1,898
Selling, general and administrative expenses	741	863	1,543	1,805
Asset impairments	4	22	9	72
Merger, restructuring, and other operating expenses, net	120	103	163	204
Legal accrual		80		80
Operating income (loss)	(51)	(185)	36	(263)
Other income (expense):				
Interest income	6	6	12	12
Interest expense	(23)	(16)	(48)	(41)
Other income (expense), net	1	(2)	2	(2)
Income (loss) before income taxes	(67)	(197)	2	(294)
Income tax expense (benefit)	(9)	(8)	15	4
Net loss	(58)	(189)	(13)	(298)
Less: Results attributable to the noncontrolling Interests		1		2
Net loss attributable to Office Depot, Inc.	\$ (58)	\$ (190)	\$ (13)	\$ (300)
Basic and diluted loss per share	\$ (0.11)	\$ (0.36)	\$ (0.02)	\$ (0.56)

*This report should be read in conjunction with the Notes to Condensed Consolidated Financial Statements herein and the Notes to Consolidated Financial Statements in the Office Depot, Inc. Form 10-K filed February 24, 2015 (the 2014 Form 10-K ).*

Table of Contents**OFFICE DEPOT, INC.****CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS****(In millions)****(Unaudited)**

	<b>13 Weeks Ended</b>		<b>26 Weeks Ended</b>	
	<b>June 27,</b>	<b>June 28,</b>	<b>June 27,</b>	<b>June 28,</b>
	<b>2015</b>	<b>2014</b>	<b>2015</b>	<b>2014</b>
Net loss	\$ (58)	\$ (189)	\$ (13)	\$ (298)
Other comprehensive income (loss), net of tax where applicable:				
Foreign currency translation adjustments	3	7	(51)	9
Other				(1)
Total other comprehensive income (loss), net of tax, where applicable	3	7	(51)	8
Comprehensive loss	(55)	(182)	(64)	(290)
Comprehensive income attributable to the noncontrolling interests		1		2
Comprehensive loss attributable to Office Depot, Inc.	\$ (55)	\$ (183)	\$ (64)	\$ (292)

*This report should be read in conjunction with the Notes to Condensed Consolidated Financial Statements herein and the Notes to Consolidated Financial Statements in the 2014 Form 10-K.*

**Table of Contents****OFFICE DEPOT, INC.****CONDENSED CONSOLIDATED BALANCE SHEETS****(In millions, except share and per share amounts)****(Unaudited)**

	<b>June 27, 2015</b>	<b>December 27, 2014</b>
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 867	\$ 1,071
Receivables, net	1,172	1,264
Inventories	1,554	1,638
Prepaid expenses and other current assets	285	245
<b>Total current assets</b>	<b>3,878</b>	<b>4,218</b>
Property and equipment, net	842	963
Goodwill	397	391
Other intangible assets, net	63	72
Timber notes receivable	915	926
Deferred income taxes	26	32
Other assets	239	242
<b>Total assets</b>	<b>\$ 6,360</b>	<b>\$ 6,844</b>
<b>Liabilities and stockholders equity</b>		
Current liabilities:		
Trade accounts payable	\$ 1,225	\$ 1,340
Accrued expenses and other current liabilities	1,227	1,517
Income taxes payable		4
Short-term borrowings and current maturities of long-term debt	59	32
<b>Total current liabilities</b>	<b>2,511</b>	<b>2,893</b>
Deferred income taxes and other long-term liabilities	602	621
Pension and postretirement obligations, net	187	196
Long-term debt, net of current maturities	648	674
Non-recourse debt	829	839
<b>Total liabilities</b>	<b>4,777</b>	<b>5,223</b>
Commitments and contingencies		
Stockholders equity:		
Common stock authorized 800,000,000 shares of \$.01 par value; issued shares 554,053,346 in June 2015 and 551,097,537 in December 2014	6	6

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Additional paid-in capital	2,582	2,556
Accumulated other comprehensive income	56	107
Accumulated deficit	(1,003)	(990)
Treasury stock, at cost 5,915,268 shares in 2015 and 2014	(58)	(58)
Total equity	1,583	1,621
Total liabilities and stockholders equity	\$ 6,360	\$ 6,844

*This report should be read in conjunction with the Notes to Condensed Consolidated Financial Statements herein and the Notes to Consolidated Financial Statements in the 2014 Form 10-K.*

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## OFFICE DEPOT, INC.

## CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In millions)

(Unaudited)

	<b>26 Weeks Ended</b>	
	<b>June 27, 2015</b>	<b>June 28, 2014</b>
<b>Cash flows from operating activities:</b>		
Net loss	\$ (13)	\$ (298)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	150	155
Charges for losses on inventories and receivables	30	35
Asset impairments	9	72
Changes in working capital and other	(311)	(126)
Net cash used in operating activities	(135)	(162)
<b>Cash flows from investing activities:</b>		
Capital expenditures	(71)	(66)
Acquisition, net of cash acquired	(10)	
Proceeds from sale of available for sale securities		43
Proceeds from assets sold and other	42	8
Net cash used in investing activities	(39)	(15)
<b>Cash flows from financing activities:</b>		
Net proceeds on employee share-based transactions	4	1
Net payments on long and short-term borrowings	(12)	(10)
Debt related fees	(1)	
Net cash used in financing activities	(9)	(9)
<b>Effect of exchange rate changes on cash and cash equivalents</b>	(21)	3
<b>Impact of cash and cash equivalent in consolidated joint-venture held for sale</b>		3
Net decrease in cash and cash equivalents	(204)	(180)
Cash and cash equivalents at beginning of period	1,071	948
Cash and cash equivalents at end of period	\$ 867	\$ 768

*This report should be read in conjunction with the Notes to Condensed Consolidated Financial Statements herein and the Notes to Consolidated Financial Statements in the 2014 Form 10-K.*





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**OFFICE DEPOT, INC.**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**(Unaudited)**

**NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Basis of Presentation:** Office Depot, Inc., including consolidated subsidiaries ( Office Depot or the Company ), is a global supplier of office products and services. The Company currently operates under the Office Depot<sup>®</sup> and OfficeMax<sup>®</sup> banners and utilizes proprietary company and product brand names. The Company's common stock is traded on the NASDAQ Global Select Market under the ticker symbol ODP. As of June 27, 2015, the Company sold to customers throughout North America, Europe, and Asia/Pacific through three reportable segments (or Divisions): North American Retail Division, North American Business Solutions Division and International Division. Refer to Note 12 for further Division information.

The Condensed Consolidated Financial Statements as of June 27, 2015 and for the 13-week and 26-week periods ended June 27, 2015 (also referred to as the second quarter of 2015 and the first half of 2015) and June 28, 2014 (also referred to as the second quarter of 2014 and the first half of 2014) are unaudited. However, in management's opinion, these financial statements reflect all adjustments of a normal recurring nature necessary to provide a fair presentation of the Company's financial position, results of operations and cash flows for the periods presented.

The Company has prepared the Condensed Consolidated Financial Statements included herein pursuant to the rules and regulations of the Securities and Exchange Commission (the SEC). Some information and note disclosures, which would normally be included in comprehensive annual financial statements prepared in accordance with accounting principles generally accepted in the United States, have been condensed or omitted pursuant to those SEC rules and regulations. For a better understanding of the Company and its Condensed Consolidated Financial Statements, we recommend reading these Condensed Consolidated Financial Statements in conjunction with the audited financial statements which are included in the 2014 Form 10-K. These interim results are not necessarily indicative of the results that should be expected for the full year.

**Cash Management:** The cash management process generally utilizes zero balance accounts which provide for the settlement of the related disbursement and cash concentration accounts on a daily basis. Trade accounts payable and Accrued expenses and other current liabilities as of June 27, 2015 and December 27, 2014 included \$57 million and \$91 million, respectively, of amounts not yet presented for payment drawn in excess of disbursement account book balances, after considering offset provisions.

At June 27, 2015, cash and cash equivalents held outside the United States amounted to \$256 million.

**Receivables under Factoring Agreement:** The Company sells selected accounts receivables on a non-recourse basis to an unrelated financial institution under a factoring agreement in France. The Company accounts for this transaction as a sale of receivables, removes receivables sold from its financial statements, and records cash proceeds when received by the Company as cash provided by operating activities in the Statements of Cash Flows. The financial institution makes available 80% of the face value of the receivables to the Company and retains the remaining 20% as a guarantee until the receipt of the proceeds associated with the factored invoices.

In the second quarter and first half of 2015, the Company withdrew \$85 million and \$179 million, respectively, from amounts available under the factoring arrangement. Receivables sold for which the Company did not obtain cash

directly from the financial institution are included in Receivables and amount to \$9 million and \$6 million as of June 27, 2015 and December 27, 2014, respectively. Retention guarantee amounts of \$8 million and \$11 million are included in Prepaid expenses and other current assets as of June 27, 2015 and December 27, 2014, respectively.

**New Accounting Standards:** In May 2014, the Financial Accounting Standards Board ( FASB ) issued an accounting standards update that will supersede most current revenue recognition guidance and modify the accounting for certain costs associated with revenue generation. The core principle of this guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The guidance provides a number of steps to apply to achieve that principle. The standard is effective for the Company's first quarter of 2017. Early adoption is not permitted. Implementation may be either through retrospective application to each period from the first quarter of 2015 or with a cumulative effect adjustment upon adoption in 2017. Additional disclosures will also be required under the new standard. In July 2015, the FASB approved a one year extension to the required implementation date but also permits companies to adopt the standard at the original effective date of 2017. The Company is assessing what impacts this new standard will have on its Consolidated Financial Statements.

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**OFFICE DEPOT, INC.**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**(Unaudited) (Continued)**

In April 2015, the FASB issued a new standard that will require debt issuance costs to be presented as a reduction of the related liability rather than as an asset. The standard is effective for the Company's first quarter of 2016 and will require prior periods to be adjusted. Early adoption is allowed. As of June 27, 2015, deferred costs of \$4 million relate to the Senior Secured Notes and will be reclassified in 2016 to reduce the carrying value of the debt and \$8 million relate to the Amended Credit Facility (as defined in Note 5), which has no outstanding borrowings and the debt issuance costs will remain classified as an asset.

In April 2015, the FASB issued a new standard that will allow companies a choice between measuring pension plan assets and liabilities based on the calendar year end date or, for companies with alternative year end dates (e.g., 52-53 week fiscal year), measurement closest to the calendar end date. The choice must be applied to all of a company's pension plans. It is effective for the Company in the first quarter of 2016; early adoption is allowed. The Company is evaluating this measurement option.

**NOTE 2. ACQUISITION AND DISPOSITIONS**

*Staples Acquisition*

On February 4, 2015, Staples, Inc. (Staples) and the Company announced that the companies have entered into a definitive merger agreement (the Staples Merger Agreement), under which Staples will acquire all of the outstanding shares of Office Depot and the Company will become a wholly owned subsidiary of Staples (the Staples Acquisition). The Company will survive the Staples Acquisition as a wholly owned subsidiary of Staples. Under the terms of the Staples Merger Agreement, Office Depot shareholders will receive, for each Office Depot share held by such shareholders, \$7.25 in cash and 0.2188 of a share in Staples common stock at closing (the Merger Consideration). Each employee share-based award outstanding at the date of the Staples Merger Agreement will vest upon the effective date of the Staples Acquisition. Upon the effective date of the Staples Acquisition, employee share-based awards subsequently granted in 2015 will be converted into a contingent right to receive the cash equivalent of the Merger Consideration subject to the same terms and conditions of the corresponding award; provided that performance and vesting periods shall be reduced in duration. The Staples Merger Agreement includes representations, warranties and conditions, including breakup fees payable or receivable under certain conditions if the transaction fails to close. Under the Staples Merger Agreement, the Senior Secured Notes will be discharged, redeemed or defeased at the Effective Time of the Staples Acquisition. The transaction has been approved by both companies' Board of Directors and was approved by Office Depot shareholders at the Company's Annual Meeting of Stockholders held on June 19, 2015. The completion of the Staples Acquisition is subject to customary closing conditions including, among others, various regulatory approvals. The transaction is expected to close by the end of calendar year 2015. Refer to the Company's definitive proxy statement filed May 18, 2015 for additional information on the transaction. Also, refer to Note 3 for expenses incurred during the second quarter and first half of 2015 related to the Staples Acquisition.

*Other*

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During the first quarter of 2015, the Company acquired an interior furniture business for \$10 million, subject to a working capital adjustment that is expected to be completed during the third quarter of 2015. The business supports the contract channel of the North American Business Solutions Division. Preliminary estimates of the fair value of assets acquired and liabilities assumed are included in the balance sheet as of June 27, 2015 and include certain amortizing intangible assets and tax-deductible goodwill, which are subject to change as integration is completed. Supplemental pro forma financial information is not provided based on materiality considerations.

*Consolidated joint venture sold*

In August 2014, the Company completed the sale of its 51% capital stock interest in Grupo OfficeMax S. de R.L. de C.V., the former OfficeMax, Incorporated ( OfficeMax ) business in Mexico, to its joint venture partner. The amounts included in the Condensed Consolidated Statements of Operations for this business are as follows:

<i>(In millions)</i>	<b>2014</b>	
	<b>Second Quarter</b>	<b>First Half</b>
Sales	\$ 59	\$ 127
Cost of goods sold and occupancy costs	(43)	(94)
Selling, general and administrative expenses	(14)	(25)
Other expenses		(2)
Income before income taxes	2	6
Income attributable to Office Depot, before income taxes	1	4

**Table of Contents****OFFICE DEPOT, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS****(Unaudited) (Continued)***Other assets held for sale*

Certain facilities identified for closure through integration and other activities have been accounted for as assets held for sale. As of June 27, 2015 and December 27, 2014, these assets amount to \$59 million and \$31 million, respectively, and are presented in Prepaid expenses and other current assets in the Condensed Consolidated Balance Sheets. Refer to Note 3 for further information on Merger, restructuring and other operating expenses, net.

**NOTE 3. MERGER, RESTRUCTURING, AND OTHER ACCRUALS**

In recent years, the Company has taken actions to adapt to changing and competitive conditions. These actions include closing facilities, consolidating functional activities, eliminating redundant positions, disposing of businesses and assets, and taking actions to improve process efficiencies. In 2013, the OfficeMax merger (the Merger) was completed and integration activities similar to the actions described above began. In mid-2014, the Company's real estate strategy (the Real Estate Strategy) identified at least 400 retail stores for closure through 2016 along with planned changes to the supply chain. The Company assumed certain restructuring liabilities previously recorded by OfficeMax.

**Merger, restructuring, and other operating expenses, net**

The Company presents Merger, restructuring and other operating expenses, net on a separate line in the Condensed Consolidated Statements of Operations to identify these activities apart from the expenses incurred to sell to and service its customers. These expenses are not included in the determination of Division operating income. The table below and narrative that follows summarize the major components of Merger, restructuring and other operating expenses, net.

<i>(In millions)</i>	<b>Second Quarter</b>		<b>First Half</b>	
	<b>2015</b>	<b>2014</b>	<b>2015</b>	<b>2014</b>
Merger related expenses				
Severance, retention, and relocation	\$ 6	\$ 48	\$ 11	\$ 119
Transaction and integration	29	38	53	59
Other related expenses	29	6	15	10
<b>Total Merger related expenses</b>	<b>64</b>	<b>92</b>	<b>79</b>	<b>188</b>
International restructuring and certain other expenses				
Severance, retention, and relocation	20	7	25	10
Integration	2	4	4	5
Other related expenses			6	1
<b>Total International restructuring and certain other expenses</b>	<b>22</b>	<b>11</b>	<b>35</b>	<b>16</b>

Staples Acquisition expenses	34	49		
Total Merger, restructuring and other operating expenses, net	\$ 120	\$ 103	\$ 163	\$ 204

Severance, retention, and relocation reflect expenses incurred for the integration of staff functions. Since the second quarter of 2014, the Real Estate Strategy has been sufficiently developed to provide a basis for estimating termination benefits for certain retail and supply chain closures that are expected to extend through 2016. Such benefits are being accrued through the anticipated employee full eligibility date. Because the specific identity of retail locations to be closed is subject to change as implementation of the Real Estate Strategy progresses, estimates are used for the store closure severance accrual. The calculation considers factors such as the expected timing of store closures, terms of existing severance plans, expected employee turnover and attrition. As the integration progresses and additional decisions about the identity and timing of closures are made, more current information will be available and assumptions used in estimating the termination benefits accrual may change.

Transaction and integration expenses include integration-related professional fees, incremental temporary contract labor, salary and benefits for employees dedicated to the Merger activity, travel costs, non-capitalizable software integration costs, and other direct costs to combine the companies. Such costs are being recognized as incurred.

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Other related expenses primarily relate to facility closure accruals, gains and losses on asset dispositions, and accelerated depreciation. Facility closure expenses include amounts incurred by the Company to close retail stores in the United States as part of the Real Estate Strategy. The Company expects to close approximately 175 retail stores in 2015 and at least 60 additional stores in 2016. The specific sites to close over this period may be influenced by real estate and other market conditions and, therefore, a reasonable estimate of future facility closure accruals cannot be made at this time. During the first quarter of 2015, the Company sold a warehouse facility that was classified as an asset held for sale at December 27, 2014. The gain of \$19 million is included in Merger, restructuring and other operating expenses, net, as the disposition was part of the supply chain integration associated with the Merger.

International restructuring and certain other expenses in 2015 include charges related to the European restructuring plan approved by the Company in 2014 to realign the organization from a geographic-focus to a business channel-focus (the European restructuring plan) and has now been approved by all countries' works councils. Both the 2015 and 2014 periods also include charges related to international organizational changes and facility closures which were started prior to the European restructuring plan. Approximately \$36 million of severance (at current exchange rates) is expected to be accrued over the remainder of 2015. Expenses for facility closures and restructuring activity will be recognized as the related accounting criteria are met.

Staples Acquisition expenses for the second quarter and first half of 2015 includes retention accruals, transaction costs and costs associated with regulatory filings. The retention amounts will be paid regardless of whether the transaction is approved and will continue to be accrued through the anticipated closing date which is expected to be before the end of 2015.

Asset impairments are not included in the table above. Refer to Note 10 for further information.

**Merger and restructuring accruals**

Of the total \$163 million Merger, restructuring and other expenses recognized in the first half of 2015 Condensed Consolidated Statement of Operations, \$112 million relates to Merger and restructuring balance sheet accruals and are included as Charges incurred in the table below. The remaining \$51 million is excluded from the table below because these items are expensed as incurred, non-cash, or otherwise not associated with Merger and restructuring balance sheet accounts.

<i>(In millions)</i>	<b>Beginning Balance</b>	<b>Charges Incurred</b>	<b>Cash Payments</b>	<b>Currency, Lease Accretion and Other Adjustments</b>	<b>Ending Balance</b>
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2015							
Termination benefits							
Merger-related accruals	\$	31	\$	13	\$ (20)	\$	24
European restructuring plan		26		18	(4)	(3)	37
Other restructuring accruals		8		6	(8)	(1)	5
		65		37	(32)	(4)	66
Lease and contract obligations, accruals for facilities closures and other costs							
Merger-related accruals		71		34	(36)		69
European restructuring plan				2	(1)	1	2
Other restructuring accruals		35		3	(9)	3	32
Acquired entity accruals		36		1	(7)		30
Staples Acquisition related accruals				35			35
		142		75	(53)	4	168
Total	\$	207	\$	112	\$ (85)	\$	234

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**OFFICE DEPOT, INC.**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**(Unaudited) (Continued)**

The \$51 million not included in the balance sheet accrual table is comprised of \$53 million Merger transaction and integration expenses, \$13 million Staples Acquisition transaction expenses, and \$4 million International restructuring integration expenses, partially offset by the \$19 million gain on the disposition of the warehouse facility associated with the supply chain integration.

**NOTE 4. INVESTMENTS**

**Boise Cascade Holdings, LLC and Boise Cascade Company Common Stock**

The Company had an investment of approximately 20% of the voting equity securities of Boise Cascade Holdings, L.L.C. ( Boise Cascade Holdings ), a building products company that originated in connection with the OfficeMax sale of its paper, forest products and timberland assets in 2004. In 2013, Boise Cascade Holdings owned common stock of Boise Cascade Company ( Boise Cascade ), a publicly traded entity, which gave the Company the indirect ownership interest of approximately 4% of the shares of Boise Cascade. During the second quarter of 2014, Boise Cascade Holdings distributed to its shareholders all of the Boise Cascade common stock it held. The Company received 1.6 million shares in this distribution, which the Company fully disposed of in open market transactions through June 28, 2014 for total cash proceeds of \$43 million. The related loss on disposal is included in Other income (expense), net in the Condensed Consolidated Statements of Operations.

**NOTE 5. DEBT**

**Amended Credit Facility**

Based on the June borrowing base certificate, at June 27, 2015, the Company had approximately \$1.2 billion of available credit under the asset-based, multi-currency revolving credit facility (the Amended Credit Facility ) provided by the Amended and Restated Credit Agreement entered into in May 2011, as amended effective February 2012, March 2013, November 2013 and May 2015. In May 2015, the Amended Credit Facility maturity date was extended from May 25, 2016 to May 25, 2017. As of June 27, 2015, letters of credit outstanding under the Amended Credit Facility totaled \$91 million. There were no borrowings under the Amended Credit Facility in the second quarter of 2015.

**Other**

Under the Staples Merger Agreement, the Senior Secured Notes will be discharged, redeemed or defeased at the Effective Time of the Staples Acquisition.

The Company was in compliance with all applicable financial covenants at June 27, 2015.

**NOTE 6. INCOME TAXES**

For the second quarter of 2015, the Company's effective tax rate was primarily impacted by valuation allowances, which limited the recognition of deferred tax benefits for pretax losses in certain tax jurisdictions while income tax expense was recognized in tax jurisdictions with pretax earnings. The effective tax rate was also impacted by nondeductible foreign interest and other nondeductible expenses. Due to the Company's valuation allowances, interim income tax reporting is likely to result in significant variability of the effective tax rate throughout the course of the year. Changes in pretax income projections and the mix of income across jurisdictions could also impact the effective tax rate each quarter.

The Company has significant deferred tax assets in the U.S. and in certain foreign jurisdictions against which valuation allowances have been established to reduce such deferred tax assets to the amount that is more likely than not to be realized. During the first quarter of 2015, the Company recognized income tax expense of \$3 million associated with the establishment of valuation allowances in certain foreign jurisdictions because the realizability of the related deferred tax assets was no longer more likely than not. As of the second quarter of 2015, valuation allowances remain in the U.S. and certain foreign jurisdictions where the Company believes it is necessary to see further positive evidence, such as sustained achievement of cumulative profits, before these valuation allowances can be released. The Company will continue to assess the realizability of its deferred tax assets.

**Table of Contents****OFFICE DEPOT, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS****(Unaudited) (Continued)**

The Company files a U.S. federal income tax return and other income tax returns in various states and foreign jurisdictions. With few exceptions, the Company is no longer subject to U.S. federal and state and local income tax examinations for years before 2014 and 2009, respectively. During the second quarter of 2015, the Company received notification that the Internal Revenue Service ( IRS ) had completed its examination of the 2013 U.S. federal income tax return with no changes. The acquired OfficeMax U.S. consolidated group is no longer subject to U.S. federal and state and local income tax examinations for years before 2010 and 2006, respectively. The U.S. federal income tax returns for 2014 and 2015 are currently under review. Generally, the Company is subject to routine examination for years 2008 and forward in its international tax jurisdictions.

Due to the completion of the IRS examination for 2013, the Company decreased its unrecognized tax benefits by \$4 million during the second quarter of 2015, which did not impact income tax expense due to an offsetting change in valuation allowance. As of the second quarter of 2015, the Company's balance of unrecognized tax benefits is \$19 million, \$6 million of which would affect the effective tax rate if recognized. It is reasonably possible that certain tax positions will be resolved within the next 12 months, which would decrease the Company's unrecognized tax benefits by \$5 million but would not affect the effective tax rate due to an offsetting change in valuation allowance. Additionally, the Company anticipates 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 be reasonably made.

**NOTE 7. STOCKHOLDERS' EQUITY**

The following table reflects the changes in stockholders' equity.

<i>(In millions)</i>	
Stockholders' equity at December 27, 2014	\$ 1,621
Net loss	(13)
Other comprehensive loss	(51)
Share transactions under employee-related plans	5
Amortization of long-term incentive stock grants	21
Stockholders' equity at June 27, 2015	\$ 1,583

Accumulated other comprehensive income (loss) activity, net of tax, where applicable, is provided in the following table:

<i>(In millions)</i>	<b>Total</b>
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	<b>Foreign Currency Translation Adjustments</b>	<b>Change in Deferred Pension</b>	
Balance at December 27, 2014	\$ 186	\$ (79)	\$ 107
Other comprehensive loss activity before reclassifications	(50)		(50)
Reclassifications from Accumulated other comprehensive income (loss) to net income			
Three month period ended March 28, 2015	(1)		(1)
Three month period ended June 27, 2015			
Net other comprehensive loss	(51)		(51)
Balance at June 27, 2015	\$ 135	\$ (79)	\$ 56

As a result of valuation allowances in the U.S. and several international taxing jurisdictions, items other than deferred pension amounts generally have little or no tax impact. The component balances are net of immaterial tax impacts, where applicable.

Table of Contents**OFFICE DEPOT, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS****(Unaudited) (Continued)****NOTE 8. EARNINGS PER SHARE**

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

<i>(In millions, except per share amounts)</i>	<b>Second Quarter</b>		<b>First Half</b>	
	<b>2015</b>	<b>2014</b>	<b>2015</b>	<b>2014</b>
<b>Basic Earnings Per Share</b>				
Numerator:				
Net loss attributable to Office Depot, Inc.	\$ (58)	\$ (190)	\$ (13)	\$ (300)
Denominator:				
Weighted-average shares outstanding	547	535	546	532
Basic loss per share	\$ (0.11)	\$ (0.36)	\$ (0.02)	\$ (0.56)
<b>Diluted Earnings Per Share</b>				
Numerator:				
Net loss attributable to Office Depot, Inc.	\$ (58)	\$ (190)	\$ (13)	\$ (300)
Denominator:				
Weighted-average shares outstanding	547	535	546	532
Effect of dilutive securities:				
Stock options and restricted stock				
Diluted weighted-average shares outstanding	547	535	546	532
Diluted loss per share	\$ (0.11)	\$ (0.36)	\$ (0.02)	\$ (0.56)

Potentially dilutive stock options and restricted stock representing 9 million shares for the second quarter and first half of 2015, and 7 million and 8 million for the second quarter and first half of 2014, respectively, were excluded from the diluted loss per share calculation because of the net loss in the periods.

Awards of options and nonvested shares representing less than 1 million additional shares of common stock were outstanding for the second quarter and first half of 2015, respectively, and 10 million and 11 million for the second quarter and first half of 2014, respectively, but were not included in the computation of diluted weighted-average shares outstanding because their effect would have been antidilutive. For the periods presented, no tax benefits have been assumed in the weighted average share calculation in jurisdictions with valuation allowances.

**NOTE 9. EMPLOYEE BENEFIT PLANS****Pension and Other Postretirement Benefit Plans North America**

The components of net periodic pension benefit for the Company's North American pension plans are as follows:

<i>(In millions)</i>	<b>Second Quarter</b>		<b>First Half</b>	
	<b>2015</b>	<b>2014</b>	<b>2015</b>	<b>2014</b>
Service cost	\$ 1	\$ 1	\$ 2	\$ 2
Interest cost	11	13	23	26
Expected return on plan assets	(14)	(16)	(28)	(31)
Net periodic pension benefit	\$ (2)	\$ (2)	\$ (3)	\$ (3)

Net periodic (benefit) cost for the Company's North American other postretirement plans were less than \$1 million.

In the first half of 2015, \$4 million of cash contributions were made to the North American pension plans. The Company expects to make additional cash contributions of \$5 million to the North American pension plans in 2015.

**Table of Contents****OFFICE DEPOT, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS****(Unaudited) (Continued)****Pension Plan Europe**

The components of net periodic pension benefit for the Company's European pension plan are as follows:

<i>(In millions)</i>	<b>Second Quarter</b>		<b>First Half</b>	
	<b>2015</b>	<b>2014</b>	<b>2015</b>	<b>2014</b>
Service cost	\$	\$	\$	\$
Interest cost	2	3	4	5
Expected return on plan assets	(3)	(4)	(7)	(7)
Net periodic pension benefit	\$ (1)	\$ (1)	\$ (3)	\$ (2)

The Company's European pension plan is in a net asset position. There are no funding requirements while this plan has an asset surplus.

Net periodic pension benefits for the North American and European pension and other postretirement benefit plans are recorded in Selling, general and administrative expenses in the Condensed Consolidated Statements of Operations.

**NOTE 10. DERIVATIVE INSTRUMENTS AND FAIR VALUE MEASUREMENTS****Derivative Instruments and Hedging Activities**

As a global supplier of office products and services the Company is exposed to risks associated with changes in foreign currency exchange rates, fuel and other commodity prices and interest rates. Depending on the exposure, settlement timeframe and other factors, the Company may enter into derivative transactions to mitigate those risks. Financial instruments authorized under the Company's established risk management policy include spot trades, swaps, options, caps, collars, forwards and futures. Use of derivative financial instruments for speculative purposes is expressly prohibited by the Company's policies. The Company may designate and account for such qualifying arrangements as hedges. As of June 27, 2015, the foreign exchange and fuel contracts extend through January 2016.

The fair values of the Company's foreign currency contracts and fuel contracts are the amounts receivable or payable to terminate the agreements at the reporting date, taking into account current interest rates, exchange rates and commodity prices. The values are based on market-based inputs or unobservable inputs that are corroborated by market data. At June 27, 2015 and December 27, 2014, Accrued expenses and other liabilities in the Condensed Consolidated Balance Sheets include \$4 million and \$6 million, respectively, related to derivative fuel contracts payable.

**Financial Instruments**



The Company measures 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. In developing its fair value estimates, the Company uses the following hierarchy:

Level 1: Quoted prices in active markets for identical assets or liabilities.

Level 2: Observable market based 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 the Company's own estimates and assumptions or those expected to be used by market participants.

The fair values of cash and cash equivalents, receivables, trade accounts payable and accrued expenses and other current liabilities approximate their carrying values because of their short-term nature.

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## OFFICE DEPOT, INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited) (Continued)

The following table presents information about financial instruments at the balance sheet dates indicated.

<i>(In millions)</i>	June 27, 2015		December 27, 2014	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Financial assets				
Timber notes receivable	\$ 915	\$ 919	\$ 926	\$ 930
Financial liabilities				
Recourse debt				
9.75% senior secured notes, due 2019	250	275	250	280
7.35% debentures, due 2016	18	18	18	18
Revenue bonds, due in varying amounts periodically through 2029	186	184	186	185
American & Foreign Power Company, Inc. 5% debentures, due 2030	14	13	14	13
Non-recourse debt	829	835	839	845

The following methods and assumptions were used to estimate the fair value of each class of financial instruments:

**Timber notes receivable:** Fair value is determined as the present value of expected future cash flows discounted at the current interest rate for loans of similar terms with comparable credit risk (Level 2 measure).

**Recourse debt:** Recourse debt for which there were no transactions on the measurement date was valued based on quoted market prices near the measurement date when available or by discounting the future cash flows of each instrument using rates based on the most recently observable trade or using rates currently offered to the Company for similar debt instruments of comparable maturities (Level 2 measure).

**Non-recourse debt:** Fair value is estimated by discounting the future cash flows of the instrument at rates currently available to the Company for similar instruments of comparable maturities (Level 2 measure).

**Fair Value Estimates Used in Impairment Analyses**North American Retail Division

As a result of declining sales in recent periods, the Company conducts a detailed quarterly store impairment analysis. The analysis uses input from retail store operations and the Company's accounting and finance personnel that organizationally report to the Chief Financial Officer. These projections are based on management's estimates of store-level sales, gross margins, direct expenses, projected store closures, exercise of future lease renewal options, and favorable lease values, where applicable. The resulting cash flows, by their nature, include judgments about how current initiatives will impact future performance. If the anticipated cash flows of a store cannot support the carrying value of its assets, the retail store operating assets, as well as the related favorable lease intangible assets, are impaired and written down to their estimated fair value using a discounted cash flow approach (a Level 3 measure).

The Company recognized store asset impairment charges of \$4 million and \$9 million, in the second quarter and first half of 2015, respectively and \$10 million and \$19 million in the second quarter and first half of 2014, respectively. The first half of 2015 charges include approximately \$1 million impairment of favorable lease intangible asset values following the identification of closing locations where future intangible asset recovery was considered unlikely. The second quarter of 2014 impairment charge includes \$1 million from a decision in March 2014 to close the Canadian stores acquired as part of the Merger.

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**OFFICE DEPOT, INC.**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**(Unaudited) (Continued)**

The second quarter of 2015 analysis incorporated the assessment of which stores are anticipated to be closed through 2016, as well as projected cash flows through the base lease period for stores identified for ongoing operations. The projections assumed declining sales in future periods. Gross margin assumptions have been held constant at current actual levels and operating costs have been assumed to be consistent with recent actual results and planned activities. For the second quarter 2015 impairment analysis, identified locations were reduced to estimated fair value of \$2 million based on their projected cash flows, discounted at 13% or estimated salvage value of \$2 million, as appropriate. Assets added to previously impaired locations, whether for Division-wide enhancements or specific location betterment, are capitalized and subsequently tested for impairment. A 100 basis point decrease in next year forecasted sales combined with a 50 basis point decrease in next year gross margin would have increased the impairment by less than \$1 million. A 100 basis point decrease in sales for all future periods would increase the impairment by approximately \$2 million. Further, an incremental 6% increase in payroll costs above the historical growth rate would increase the impairment by \$6 million.

The Company will continue to evaluate initiatives to improve performance and lower operating costs. To the extent that forward-looking sales and operating assumptions are not achieved and are subsequently reduced, or in certain circumstances, even if store performance is as anticipated, additional impairment charges may result. However, at the end of the second quarter of 2015, the impairment analysis reflects the Company's best estimate of future performance.

**Other assets**

Other asset impairment charges for the second quarter of 2014 include \$12 million following a decision to convert certain websites to a common platform. The impairment amount was based on a cash flow analysis over the remaining use period. The first half of 2014 also includes an additional \$28 million charge related to the abandonment of a software implementation project in Europe and \$13 million for the write off of capitalized software following certain information technology platform decisions related to the Merger. These charges are included in the Asset impairments line in the Condensed Consolidated Statements of Operations.

**NOTE 11. COMMITMENTS AND CONTINGENCIES**

**Legal Matters**

The Company is involved in litigation arising in the normal course of 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), the Company does not believe that contingent liabilities related to these matters (including the matters discussed below), either individually or in the aggregate, will materially affect the Company's financial position, results of operations or cash flows.

On February 4, 2015, Staples and Office Depot entered into the Staples Merger Agreement under which the companies would combine in a stock and cash transaction. On February 9, 2015, a putative class action lawsuit was filed by purported Office Depot shareholders in the Court of Chancery of the State of Delaware ( Court ) challenging

the transaction and alleging that the defendant companies Office Depot, Staples, Merger Sub, and Starboard Value LP and individual members of Office Depot's Board of Directors violated applicable laws by breaching their fiduciary duties and/or aiding and abetting such breaches. The plaintiffs in David Raul, v. Office Depot, Inc. et al. seek, among other things, injunctive relief and rescission, as well as fees and costs. Subsequently, eight other lawsuits were filed in the Court of Chancery of the State of Delaware making similar allegations, namely Beth Koeneke v. Office Depot, Inc. et al., Jamison Miller v. Office Depot, Inc. et al., Eric R. Gilbert v. Office Depot, Inc. et al., The Feivel and Helene Gottlieb Defined Benefit Pension Plan v. Office Depot, et al., Charles Miller v. Smith et al., David Max v. Office Depot, Inc. et al., Patrick Connors v. Office Depot, Inc. and Steve Renous v. Smith et al. The Court subsequently consolidated all of the Delaware cases and named Jamison Miller and Steve Renous as co-plaintiffs and ordered the plaintiffs to file an amended consolidated complaint. The consolidated case is named In re Office Depot, Inc. Stockholders Litigation Consolidated, C.A. No. 10655-CB. After limited discovery, the plaintiffs and defendants agreed on certain additional disclosures to the Company's definitive proxy statement filed on May 18, 2015, which were made in an 8-K filing on June 5, 2015, and the plaintiffs withdrew from the calendar their planned motion to preliminarily enjoin the stockholder vote on the merger. The parties have agreed that the defendants need not respond to the current complaint. Additionally, in February 2015, two lawsuits were filed in Palm Beach County Circuit Court, namely Keny Petit-Frere v. Office Depot, Inc., et al. and John Sweatman v. Office Depot, Inc., et al. making the same allegations as in the Delaware actions. The lawsuits generally sought injunctive relief enjoining the consummation of the transaction, rescission of the transaction in the event it is consummated, damages, fees, costs, and other remedies. Office Depot filed a motion to dismiss the Florida lawsuits for improper venue, and that motion was granted on May 15, 2015.

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**Table of Contents****OFFICE DEPOT, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS****(Unaudited) (Continued)**

In addition, in the ordinary course of business, sales to and transactions with government customers may be subject to lawsuits, investigations, audits and review by governmental authorities and regulatory agencies, with which the Company cooperates. Many of these lawsuits, investigations, audits and reviews are resolved without material impact to the Company. While claims in these matters may at times assert large demands, the Company does not believe that contingent liabilities related to these matters, either individually or in the aggregate, will materially affect its financial position, results of operations or cash flows. In addition to the foregoing in 2009, State of California et al., ex rel. David Sherwin v. Office Depot, Inc. (the Sherwin lawsuit ) was filed in Superior Court for the State of California, Los Angeles County, and unsealed on October 16, 2012. The lawsuit asserted claims, including claims under the California False Claims Act, based on allegations regarding certain pricing practices under now expired agreements that were in place between 2001 and January 1, 2011, pursuant to which governmental agencies purchased office supplies from us. The plaintiffs sought monetary damages and other relief, including trebling of damages and statutory penalties. On June 25, 2014, the Company participated in a non-binding, voluntary mediation in which the Company negotiated a potential settlement to resolve the matter. During the second quarter of 2014, the Company recorded an \$80 million incremental increase to the legal accrual which included the potential settlement, as well as attorneys' fees and other related legal matters. On December 19, 2014, Office Depot and the plaintiffs executed a Settlement Agreement to resolve the lawsuit. Pursuant to the terms of the Settlement Agreement, the Company agreed to pay the plaintiffs \$68 million to settle the matter (the Settlement Amount ), as well as \$9 million in legal fees, costs, and expenses. In exchange for, and in consideration of, the Company's agreement to pay the Settlement Amount, the plaintiffs agreed to dismiss their action against the Company with prejudice. In February 2015, the court entered orders approving the settlement and dismissing the case with prejudice. The Settlement Amount was subsequently placed in escrow pursuant to the Settlement Agreement and, during the second quarter of 2015, was released from escrow and disbursed in accordance with the terms of the court's orders.

In addition to the foregoing, Heitzenrater v. OfficeMax North America, Inc., et al. was filed in the United States District Court for the Western District of New York in September 2012 as a putative class action alleging violations of the Fair Labor Standards Act and New York Labor Law. The complaint alleges that OfficeMax misclassified its assistant store managers ( ASMs ) as exempt employees. The Company believes that adequate provisions have been made for probable losses and such amounts are not material. However, in light of the early stage of the case and the inherent uncertainty of litigation, the Company is unable to estimate a reasonably possible range of loss in the matter. OfficeMax intends to vigorously defend itself in this lawsuit. Further, Kyle Rivet v. Office Depot, Inc., formerly known as Constance Gibbons v. Office Depot, Inc., a putative class action that was instituted in May 2012, is pending in the United States District Court for the District of New Jersey. The complaint alleges that Office Depot's use of the fluctuating workweek (FWW) method of pay was unlawful because Office Depot failed to pay a fixed weekly salary and failed to provide its ASMs with a clear and mutual understanding notification that they would receive a fixed weekly salary for all hours worked. The plaintiffs in both complaints seek unpaid overtime, punitive damages, and attorneys' fees. The Company believes in this case that adequate provisions have been made for probable losses and such amounts are not material. However, in light of the early stage of the case and the inherent uncertainty of litigation, the Company is unable to estimate a reasonably possible range of loss in these matters. Office Depot intends to vigorously defend itself in these lawsuits.

OfficeMax is named a defendant in a number of lawsuits, claims, and proceedings arising out of the operation of certain paper and forest products assets prior to those assets being sold in 2004, for which OfficeMax agreed to retain responsibility. Also, as part of that sale, OfficeMax agreed to retain responsibility for all pending or threatened proceedings and future proceedings alleging asbestos-related injuries arising out of the operation of the paper and forest products assets prior to the closing of the sale. The Company has made provision for losses with respect to the pending proceedings. Additionally, as of June 27, 2015, our estimate of the range of reasonably possible losses for environmental liabilities with respect to certain sites where hazardous substances or other contaminants are or may be located was approximately \$10 million to \$25 million. The Company regularly monitors its estimated exposure to these liabilities. As additional information becomes known, these estimates may change, however, the Company does not believe any of these OfficeMax retained proceedings are material to the Company's business.

Table of Contents**OFFICE DEPOT, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS****(Unaudited) (Continued)****NOTE 12. DIVISION INFORMATION**

The Company has three reportable segments: North American Retail Division, North American Business Solutions Division, and International Division. The North American Retail Division includes retail stores in the United States, including Puerto Rico and the U.S. Virgin Islands, which offer office supplies, technology products and solutions, business machines and related supplies, facilities products, and office furniture. Most stores also have a copy and print center offering printing, reproduction, mailing and shipping. The North American Business Solutions Division sells office supply products and services in Canada and the United States, including Puerto Rico and the U.S. Virgin Islands. North American Business Solutions Division customers are served through dedicated sales forces, through catalogs, telesales, and electronically through its Internet sites. The International Division sells office products and services through direct mail catalogs, contract sales forces, Internet sites, and retail stores in Europe and Asia/Pacific.

The former OfficeMax business in Mexico is presented as Other. The integration of this business into the International Division was suspended in the second quarter of 2014 due to its sale, and it was managed and reported independently of the Company's other international businesses, through the date of the sale.

The office supply products and services offered across all operating segments are similar. Division operating income is determined based on the measure of performance reported internally to manage the business and for resource allocation. This measure charges to the respective Divisions those expenses considered directly or closely related to their operations and allocates support costs. Certain operating expenses and credits are not allocated to the Divisions including Asset impairments and Merger, restructuring and other operating expenses, net, as well as expenses and credits retained at the Corporate level, including certain management costs and legacy pension and environmental matters. Other companies may charge more or less of these items to their segments and results may not be comparable to similarly titled measures used by other entities.

The following is a summary of Sales and Division operating income (loss) by each of the Divisions, reconciled to consolidated totals.

<i>(In millions)</i>	<b>Sales</b>			
	<b>Second Quarter</b>		<b>First Half</b>	
	<b>2015</b>	<b>2014</b>	<b>2015</b>	<b>2014</b>
North American Retail Division	\$ 1,342	\$ 1,457	\$ 2,995	\$ 3,267
North American Business Solutions Division	1,434	1,491	2,910	3,032
International Division	664	834	1,412	1,768
Other		59		127
<b>Total</b>	<b>\$ 3,440</b>	<b>\$ 3,841</b>	<b>\$ 7,317</b>	<b>\$ 8,194</b>



<i>(In millions)</i>	<b>Division Operating Income (Loss)</b>			
	<b>Second Quarter</b>		<b>First Half</b>	
	<b>2015</b>	<b>2014</b>	<b>2015</b>	<b>2014</b>
North American Retail Division	\$ 42	\$ (6)	\$ 128	\$ 31
North American Business Solutions Division	63	59	120	99
International Division	2	(2)	15	14
Total	\$ 107	\$ 51	\$ 263	\$ 144

**Table of Contents****OFFICE DEPOT, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS****(Unaudited) (Continued)**

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

<i>(In millions)</i>	<b>Second Quarter</b>		<b>First Half</b>	
	<b>2015</b>	<b>2014</b>	<b>2015</b>	<b>2014</b>
Total Division operating income	\$ 107	\$ 51	\$ 263	\$ 144
Add/(subtract):				
Other operating income		2		8
Asset impairments	(4)	(22)	(9)	(72)
Merger, restructuring, and other operating expenses, net	(120)	(103)	(163)	(204)
Legal accrual		(80)		(80)
Unallocated expenses	(34)	(33)	(55)	(59)
Interest income	6	6	12	12
Interest expense	(23)	(16)	(48)	(41)
Other income (expense), net	1	(2)	2	(2)
Income (loss) before income taxes	\$ (67)	\$ (197)	\$ 2	\$ (294)

The gross amount of goodwill and the amount of accumulated impairment losses as of June 27, 2015 and December 27, 2014 are provided in the following table:

<i>(In millions)</i>	<b>North American Retail Division</b>	<b>North American Business Solutions Division</b>	<b>International Division</b>	<b>Total</b>
	Goodwill	\$ 80	\$ 647	\$ 922
Accumulated impairment losses	(2)	(349)	(907)	(1,258)
Balance as of December 27, 2014	78	298	15	391
Additions		6		6
Balance as of June 27, 2015	\$ 78	\$ 304	\$ 15	\$ 397

Refer to Note 2 for additional information on goodwill associated with the first quarter 2015 additions.



**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.****Acquisition by Staples**

On February 4, 2015, Staples and the Company announced that the companies have entered into a definitive merger agreement (the Staples Merger Agreement), under which Staples will acquire all of the outstanding shares of Office Depot and the Company will become a wholly owned subsidiary of Staples (the Staples Acquisition). Under the terms of the Staples Merger Agreement, Office Depot shareholders will receive, for each Office Depot share held by such shareholders, \$7.25 in cash and 0.2188 of a share in Staples common stock at closing (the Merger Consideration). Each employee share-based award outstanding at the date of the Staples Merger Agreement will vest upon the effective date of the Staples Acquisition. Upon the effective date of the Staples Acquisition, employee share-based awards subsequently granted in 2015 will be converted into a contingent right to receive the cash equivalent of the Merger Consideration subject to the same terms and conditions of the corresponding award; provided that performance and vesting periods shall be reduced in duration. The transaction has been approved by both companies Board of Directors and was approved by the Office Depot shareholders at the Company's Annual Meeting of Stockholders held on June 19, 2015. The completion of the Staples Acquisition is subject to customary closing conditions including, among others, various regulatory approvals. Under the Staples Merger Agreement the Senior Secured Notes will be discharged, redeemed or defeased at the Effective Time of the Staples Acquisition. The transaction is expected to close by the end of the calendar year 2015. Refer to the Company's definitive proxy statement filed May 18, 2015 for additional information on the transaction. We cannot guarantee that the Staples Acquisition will be completed or that, if completed, it will be exactly on the terms as set forth in the Staples Merger Agreement. Should the Staples Acquisition not be completed, the Company will continue to be responsible for payment of commitments to current employees under retention arrangements and may either receive or pay a breakup fee, as provided for in the Staples Merger Agreement.

**RESULTS OF OPERATIONS****OVERVIEW**

Office Depot, Inc., together with its subsidiaries (Office Depot or the Company), is a global supplier of office products and services to consumers and businesses of all sizes. We sell to customers throughout North America, Europe, and Asia/Pacific through three reportable segments (or Divisions): North American Retail Division, North American Business Solutions Division and International Division. The North American Retail Division includes our retail stores in the United States, including Puerto Rico and the U.S. Virgin Islands, which offer office supplies, technology products and solutions, business machines and related supplies, facilities products, and office furniture. Most stores also have a copy and print center offering printing, reproduction, mailing and shipping services. The North American Business Solutions Division sells office supply products and services in Canada and the United States, including Puerto Rico and the U.S. Virgin Islands. North American Business Solutions Division customers are served through dedicated sales forces, catalogs, telesales, and electronically through our Internet sites. Our International Division sells office products and services through direct mail catalogs, contract sales forces, Internet sites, and retail stores in Europe and Asia/Pacific. The former OfficeMax, Incorporated (OfficeMax) business in Mexico is presented as an Other segment. The integration of this business, into the International Division was suspended in the second quarter of 2014 due to the sale and it was managed and reported independently of the Company's other international businesses, through the date of the sale.

Management's Discussion and Analysis of Financial Condition and Results of Operations (MD&A) is intended to provide information to assist readers in better understanding and evaluating our financial condition and results of operations. We recommend reading this MD&A in conjunction with our Condensed Consolidated Financial

## Edgar Filing: OFFICE DEPOT INC - Form 10-Q

Statements and the Notes to those statements included in Item 1 of this Quarterly Report on Form 10-Q, as well as our 2014 Annual Report on Form 10-K, filed with the U.S. Securities and Exchange Commission (the SEC ) on February 24, 2015 (the 2014 Form 10-K ).

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, c expressions in this Quarterly Report on Form 10-Q, 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 our 2014 Form 10-K, and Forward-Looking Statements, found in Part I of our 2014 Form 10-K, apply to these forward-looking statements.

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A summary of certain factors impacting results for the 13-week and 26-week periods ended June 27, 2015 (also referred to as the second quarter of 2015 and the first half of 2015) and June 28, 2014 (also referred to as the second quarter of 2014 and the first half of 2014) is provided below. Additional discussion of the 2015 second quarter and first half results is provided in the narrative that follows this overview.

In mid-2014, the Company's real estate strategy (the Real Estate Strategy) identified at least 400 retail stores for closure through 2016, along with planned changes to the supply chain. Sales reported for the second quarter and first half of 2015 compared to the same periods of the prior year were significantly affected by planned store closures in North America, as well as changes in currency exchange rates abroad.

<i>(In millions)</i>	Second Quarter			First Half		
	2015	2014	Change	2015	2014	Change
North American Retail Division	\$ 1,342	\$ 1,457	(8)%	\$ 2,995	\$ 3,267	(8)%
<i>Change in comparable store sales</i>			1%			(1)%
North American Business Solutions Division	1,434	1,491	(4)%	2,910	3,032	(4)%
<i>Change in constant currencies</i>			(3)%			(3)%
International Division	664	834	(20)%	1,412	1,768	(20)%
<i>Change in constant currencies</i>			(6)%			(7)%
Other		59			127	
Total	\$ 3,440	\$ 3,841	(10)%	\$ 7,317	\$ 8,194	(11)%

Gross margin increased 67 basis points in the second quarter of 2015 compared to the same period of 2014, with increases both in North American Retail and International Divisions and a slight decrease in the North American Business Solutions Division. In the first half of 2015, gross margin increased 77 basis points, compared to the first half of 2014, with increases across all three Divisions.

Total Company Selling, general and administrative expenses decreased in 2015 compared to 2014, reflecting the closure of stores in North America, lower payroll and advertising expenses, operational efficiencies and synergies, the 2014 sale of the business in Mexico, and foreign currency translation effects. As a percentage of sales, total Company Selling, general and administrative expenses decreased in both the second quarter and first half of 2015 compared to 2014 by over 90 basis points.

Non-cash asset impairment charges of \$4 million and \$9 million were recorded in the second quarter and first half of 2015, respectively. Non-cash asset impairment charges for the second quarter and first half of 2014 were \$22 million and \$72 million, respectively. All periods include charges related to underperforming stores in North America. Additionally, the 2014 charges reflect the abandonment and impairment of certain software projects and assets related to the OfficeMax merger (the Merger).

We recognized \$120 million and \$163 million of Merger, restructuring, and other operating expenses, net in the second quarter and first half of 2015, respectively, compared to \$103 million and \$204 million in the

second quarter and first half of 2014, respectively. In the second quarter of 2015, this line item includes \$64 million of expenses related to Merger activities, \$22 million of International restructuring and certain other operating expenses, and \$34 million related to the Staples Acquisition. Additional integration and restructuring expenses are expected to be incurred in 2015 and 2016.

The effective tax rates of 13% and 750% for the second quarter and first half of 2015, respectively, reflect the impact of valuation allowances limiting recognition of deferred tax assets. Because of the valuation allowances and changes in the mix of earnings among jurisdictions and during interim periods, the Company continues to experience significant effective tax rate volatility within the year and across years.

Loss per share was \$(0.11) in the second quarter of 2015 compared to \$(0.36) in the second quarter of 2014. Loss per share was \$(0.02) in the first half of 2015 compared to \$(0.56) in the first half of 2014.

At June 27, 2015, we had \$867 million in cash and cash equivalents and \$1.2 billion available under the Amended Credit Agreement. Cash used in operating activities was \$135 million for the first half of 2015, compared to a use of \$162 million in the same period of the prior year.

**Table of Contents****OPERATING RESULTS**

Discussion of additional income and expense items, including material charges and credits and changes in interest and income taxes follows our review of segment results.

In the Division tables that follow, the changes in Sales for 2014 reflect the impact of adding the OfficeMax business.

**NORTH AMERICAN RETAIL DIVISION**

<i>(In millions)</i>	<b>Second Quarter</b>		<b>First Half</b>	
	<b>2015</b>	<b>2014</b>	<b>2015</b>	<b>2014</b>
Sales	\$ 1,342	\$ 1,457	\$ 2,995	\$ 3,267
% change	(8)%	55%	(8)%	57%
Division operating income (loss)	\$ 42	\$ (6)	\$ 128	\$ 31
% of sales	3%	%	4%	1%
Comparable store sales increase (decline)	1%	(2)%	(1)%	(2)%

Sales in our North American Retail Division decreased 8% in the second quarter of 2015 compared to sales in the same period last year. The decrease resulted primarily from store closures associated with the Real Estate Strategy. While store closures result in lower sales in the North American Retail Division, they are typically lower performing stores and future Division operating income may benefit. Comparable store sales in the second quarter of 2015 increased 1%, reflecting benefits from sales transfer from closed stores and increased operational effectiveness. Transaction counts increased and average order value decreased slightly. The increase in comparable store sales reflect sales increases in Copy and Print Depot, furniture, and supplies, partially offset by decreases in sales of technology products and technology-related items.

Comparable store sales are based on stores that have been open for at least one year. Stores are removed from the comparable sales calculation one month prior to closing, as sales during that period are largely non-comparable clearance activity, and during periods of store remodeling and if significantly downsized. As the Company continues to implement the Real Estate Strategy, current period comparable store sales calculations are positively affected as customers transfer from closed to nearby stores which remain open. The average sales transfer rate achieved to date under the Real Estate Strategy is estimated to be at least 30%.

The North American Retail Division reported operating income of \$42 million in the second quarter of 2015, compared to an operating loss of \$6 million in the same period of prior year. Store closures contributed to declines in occupancy, payroll and other store operating costs. During the second quarter of 2015, the Division recognized \$15 million in favorable legal settlements relating to certain product manufacturers pricing practices. Beyond the impact from store closures, operating costs decreased from lower advertising and payroll expenses. Partially offsetting these benefits, Division operating profit was negatively affected by the sales decline on recovery of fixed operating expenses (the flow through impact).

The factors discussed above affecting the second quarter of 2015 are also reflective of those impacting the first half of 2015 compared to the same period of 2014. The sales decline reflects the impact of closing stores as outlined in the Real Estate Strategy. The transfer of sales from closing stores to locations that remain open has had a positive impact on comparable store sales. Also, operating expenses have decreased from the store closures and continued synergy impacts from the Merger.



During the second quarter of 2015, the North American Retail Division closed 99 stores, ending the period with a store count of 1,626.

The Company expects to close approximately 175 stores in 2015. Consistent with the Real Estate Strategy announced in 2014, at least an additional 60 stores are anticipated to be closed in 2016, bringing the total closures to at least 400 stores over the 2014 to 2016 integration period. The closures in 2015 and 2016 are expected to result in exit costs associated with facility closures and severance. Charges associated with these decisions will be reported as appropriate in Asset impairments and Merger, restructuring and other operating expenses, net in the Consolidated Statements of Operations. These charges will be reflected in Corporate reporting, and not included in the determination of Division income in future periods.

**Table of Contents****NORTH AMERICAN BUSINESS SOLUTIONS DIVISION**

<i>(In millions)</i>	<b>Second Quarter</b>		<b>First Half</b>	
	<b>2015</b>	<b>2014</b>	<b>2015</b>	<b>2014</b>
Sales	\$ 1,434	\$ 1,491	\$ 2,910	\$ 3,032
% change	(4)%	91%	(4)%	90%
Division operating income (loss)	\$ 63	\$ 59	\$ 120	\$ 99
% of sales	4%	4%	4%	3%

Sales in our North American Business Solutions Division in U.S. dollars decreased 4% in the second quarter of 2015 compared to the same period in the prior year. On a constant currency basis, sales decreased 3%. Sales decreased in the contract channel and increased in the direct channel.

The decline in the contract channel sales reflects the continued transition out of certain customers that purchased under a legacy OfficeMax buying arrangement with a Minority Women Business Enterprise (a Tier 1 buying arrangement) that was modified in 2014, the negative impacts from changes in Canadian currency exchange rates, and the closure during the second quarter of 2014 of all 19 stores in Canada (the sales of which were reported in the contract channel). The negative impact from the legacy OfficeMax Tier 1 buying arrangement is expected to continue through the remainder of 2015. In the direct channel, online sales increased during the second quarter of 2015, reflecting benefits from an enhanced Internet shopping offering and experience. The increased online sales were substantially offset by reduced catalog and call center sales. We anticipate this shift in customer shopping preference will continue. On a product category basis for the Division, sales in cleaning and breakroom and Copy and Print Depot increased while sales of supplies and technology products decreased.

Division operating income for the second quarter 2015 was \$63 million, compared to \$59 million in the same period of the prior year. Division operating income as a percentage of sales was slightly higher in the second quarter of 2015 compared to the same period in 2014. The improvement reflects a decrease in operating expenses, including lower payroll, advertising and allocated general and administrative expenses, and benefits from closing the stores in Canada, partially offset by the flow through impact of lower sales.

The factors discussed above affecting the second quarter of 2015 are also reflective of those impacting the first half of 2015 compared to the same period of 2014. The sales decline reflects the impact of customer attrition, changes in foreign currency exchange rates and the 2014 closure of stores in Canada. Also, operating expenses have decreased from continued synergy impacts from the Merger and the Canadian store closures.

**INTERNATIONAL DIVISION**

<i>(In millions)</i>	<b>Second Quarter</b>		<b>First Half</b>	
	<b>2015</b>	<b>2014</b>	<b>2015</b>	<b>2014</b>
Sales	\$ 664	\$ 834	\$ 1,412	\$ 1,768
% change	(20)%	19%	(20)%	21%
Division operating income (loss)	\$ 2	\$ (2)	\$ 15	\$ 14
% of sales	%	%	1%	1%

Sales in our International Division in U.S. dollars decreased 20% in the second quarter of 2015 compared to sales in the same period of the prior year. On a constant currency basis, sales decreased 6%. Constant currency sales were

lower in the contract and direct channels and higher in the retail channel. The contract channel sales decline reflects competitive factors that contributed to the loss of certain customers and a decline in orders from existing and new customers in the larger European markets. Sales were also negatively affected by sales force vacancies in certain locations in reaction to the European restructuring plan announced in late 2014. These declines were partially offset by sales increases in Asia and smaller European markets. In the direct channel, catalog and call center sales continued to decline across all product categories, partially offset by an increase in online sales. This change in customer buying preference has been ongoing and is expected to continue. Retail sales in constant currencies reflect higher sales in Korea and Sweden.

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Division operating income totaled \$2 million in the second quarter of 2015 compared to an operating loss of \$2 million in the second quarter of 2014. Division operating income as a percentage of sales was slightly positive in the second quarter of 2015 compared to slightly negative in the same period of 2014. Operating expenses decreased across the Division, reflecting lower payroll and advertising expenses. Supply chain expenses decreased from facility closures and lower volume. The lower operating costs more than offset the flow through impact of lower sales.

The European restructuring plan has been approved by all countries' works councils and is expected to be substantially complete by the end of 2015. The Company expects to generate the same local currency annual cost reduction benefits by the end of 2016, as previously communicated in October 2014, which translates to approximately \$80 million at current exchange rates. Costs associated with restructuring activities are reported at the Corporate level and discussed in the Restructuring and other operating expenses, net section below.

For U.S. reporting, the International Division's sales are translated into U.S. dollars at average exchange rates experienced during the period. The Division's reported sales were negatively affected by \$119 million and \$236 million from changes in foreign currency exchange rates in the second quarter and first half of 2015, respectively. However, the changes in foreign currency exchange rates did not have a significant impact on Division operating income. We analyze our international operations in terms of local currency performance to allow focus on operating trends and results.

The factors discussed above affecting the second quarter of 2015 are also reflective of those impacting the first half of 2015 compared to the same period of 2014. Sales reported in U.S. dollars were reduced by changes in foreign currency exchange rates. Constant currency sales declines in the contract and direct channels reflect customer attrition and changes in customer buying preferences. The decline in sales was more than offset by lower operating expenses.

**OTHER**

<i>(In millions)</i>	2014	
	Second Quarter	First Half
Sales	\$ 59	\$ 127
Other operating income	\$ 2	\$ 8

With the Merger, we acquired the OfficeMax joint venture business operating in Mexico, Grupo OfficeMax S. de R.L. de C.V. ( Grupo OfficeMax ). In August 2014, we completed the sale of our interest in this business to our joint venture partner. In the second quarter of 2014, the integration of this business into the International Division was suspended, and subsequently managed and reported independently of the Company's other international businesses.

Since the Company controlled the joint venture, the total Grupo OfficeMax results through the date of the sale are included in the Consolidated Statement of Operations, with an apportionment of the period results to the noncontrolling interest based on their ownership percentage.

**CORPORATE**

The line items in our Condensed Consolidated Statements of Operations impacted by these Corporate activities are presented in the table below, followed by a narrative discussion of the significant matters. These activities are managed at the Corporate level and, accordingly, are not included in the determination of Division income for management reporting or external disclosures.

<i>(In millions)</i>	<b>Second Quarter</b>		<b>First Half</b>	
	<b>2015</b>	<b>2014</b>	<b>2015</b>	<b>2014</b>
Asset impairments	\$ 4	\$ 22	\$ 9	\$ 72
Merger, restructuring, and other operating expenses, net	120	103	163	204
Legal accrual		80		80
Total charges and credits impact on Operating income (loss)	\$ 124	\$ 205	\$ 172	\$ 356

In addition to these charges and credits, certain Selling, general and administrative expenses are not allocated to the Divisions and are managed at the Corporate level. Those expenses are addressed in the section Unallocated Costs below.

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**Asset Impairments, Merger, Restructuring, Other Charges and Credits**

In recent years, we have taken actions to adapt to changing and competitive conditions. These actions include closing stores and distribution centers, consolidating functional activities, disposing of businesses and assets, and improving process efficiencies. We have also recognized significant asset impairment charges related to stores and intangible assets and significant expenses associated with the Merger and integration and, in 2015, began recognizing costs associated with the Staples Acquisition. These expense items are expected to continue in future periods.

**Asset Impairments**

We recognized asset impairment charges of \$4 million and \$9 million in the second quarter and first half of 2015, respectively, and \$22 and \$72 million in the second quarter and first half of 2014, respectively. The 2015 charges relate to impairments of store operating assets, as well as impairment of certain favorable lease assets following identification of closing locations where future intangible asset recovery was considered unlikely. The second quarter of 2014 impairment charge includes \$10 million related to store impairments and \$12 million resulting from a decision to convert certain websites to a common platform. The asset impairment charges for the first half of 2014 also include \$28 million related to the abandonment of a software implementation project in Europe, \$13 million to write off capitalized software following certain information technology platform decisions related to the Merger and \$1 million from a decision in March 2014 to close the 19 stores in Canada acquired as part of the Merger.

The second quarter 2015 analysis incorporated the assessment of which stores are anticipated to be closed through 2016, as well as projected cash flows through the base lease period for stores identified for ongoing operations. The projections assumed declining sales in future periods. Gross margin assumptions have been held constant at current actual levels and operating costs have been assumed to be consistent with recent actual results and planned activities. For the second quarter 2015 impairment analysis, identified locations were reduced to estimated fair value of \$2 million based on their projected cash flows, discounted at 13% or estimated salvage value of \$2 million, as appropriate. Assets added to previously impaired locations, whether for Division-wide enhancements or specific location betterment, are capitalized and subsequently tested for impairment. A 100 basis point decrease in next year forecasted sales combined with a 50 basis point decrease in next year gross margin would have increased the impairment by less than \$1 million. A 100 basis point decrease in sales for all future periods would increase the impairment by approximately \$2 million. Further, an incremental 6% increase in payroll costs above the historical growth rate would increase the impairment by \$6 million.

The Company will continue to evaluate initiatives to improve performance and lower operating costs. To the extent that forward-looking sales and operating assumptions are not achieved and are subsequently reduced, or in certain circumstances, even if store performance is as anticipated, additional impairment charges may result. However, at the end of the second quarter of 2015, the impairment analysis reflects the Company's best estimate of future performance.

As implementation of the Retail Strategy progresses, we are likely to experience volatility in results. In addition to charges for severance, and facility closure costs that will be recognized as decisions are made, we may experience volatility from the timing of recognition of impairment charges followed by credits related to capital leases and deferred rent accounts when the leases are terminated or modified.

**Table of Contents*****Merger, restructuring and other operating expenses, net***

The table below summarizes the major components of Merger, restructuring and other operating expenses, net.

<i>(In millions)</i>	<b>Second Quarter</b>		<b>First Half</b>	
	<b>2015</b>	<b>2014</b>	<b>2015</b>	<b>2014</b>
<b>Merger related expenses</b>				
Severance, retention, and relocation	\$ 6	\$ 48	\$ 11	\$ 119
Transaction and integration	29	38	53	59
Other related expenses	29	6	15	10
<b>Total Merger related expenses</b>	<b>64</b>	<b>92</b>	<b>79</b>	<b>188</b>
<b>International restructuring and certain other expenses</b>				
Severance, retention, and relocation	20	7	25	10
Integration	2	4	4	5
Other related expenses			6	1
<b>Total International restructuring and certain other expenses</b>	<b>22</b>	<b>11</b>	<b>35</b>	<b>16</b>
<b>Staples Acquisition expenses</b>	<b>34</b>		<b>49</b>	
<b>Total Merger, restructuring and other operating expenses, net</b>	<b>\$ 120</b>	<b>\$ 103</b>	<b>\$ 163</b>	<b>\$ 204</b>

***Merger-related expenses***

Expenses include severance, employee retention, integration-related professional fees, incremental temporary contract labor, salary and benefits for employees dedicated to Merger activity, travel and relocation costs, non-capitalizable software integration costs, facility closure accruals, gains and losses on asset dispositions, accelerated depreciation, and other direct costs to combine the companies. During the first quarter of 2015, the Company sold a warehouse facility that was classified as held for sale at December 27, 2014. The gain is included in Other related expenses because the disposition was part of the supply chain integration associated with the Merger.

It is expected that significant Merger-related expenses will continue to be incurred in future periods as decisions are made about facility closures, organizational structure and other integration activities in 2015 and 2016, and will be recognized in future periods as the related accounting criteria are met.

***International restructuring and certain other expenses, net***

International restructuring and certain other expenses in 2015 include charges related to the European restructuring plan approved in 2014 to realign the organization from a geographic-focus to a business channel-focus (the European restructuring plan). Both the 2015 and 2014 periods include charges related to international organizational changes and facility closures which were started prior to the European restructuring plan. The European restructuring plan has been approved by all countries' works councils. Approximately \$36 million of severance (at current exchange rates) is expected to be accrued over the remainder of 2015. Expenses for facility closures and restructuring activity will be recognized as the related accounting criteria are met.

*Staples Acquisition Expenses*

During the second quarter and first half of 2015, the Company incurred \$34 million and \$49 million, respectively, of retention accruals, transaction costs and costs associated with regulatory filings. The retention amounts will be paid regardless of whether the transaction is approved and will continue to be accrued through the anticipated closing date, which is expected to be before the end of 2015.

Refer to Notes 2 and 3 of the Notes to the Condensed Consolidated Financial Statements for additional information



**Table of Contents****Legal Accrual**

In June 2014, the Company participated in a non-binding, voluntary mediation in which the Company negotiated a potential settlement to resolve the Sherwin lawsuit. During the second quarter of 2014, the Company recorded an \$80 million incremental increase to the legal accrual which included the potential settlement, as well as attorneys' fees and other related legal matters. On December 19, 2014, Office Depot and the plaintiffs executed a Settlement Agreement to resolve the lawsuit. Pursuant to the terms of the Settlement Agreement, the Company agreed to pay the plaintiffs \$68 million to settle the matter (the Settlement Amount), as well as \$9 million in legal fees, costs, and expenses. In exchange for, and in consideration of, the Company's agreement to pay the Settlement Amount, the plaintiffs agreed to dismiss their action against the Company with prejudice. In February 2015, the court entered orders approving the settlement and dismissing the case with prejudice. The Settlement Amount and the related fees were paid during the second quarter of 2015.

**Unallocated Expenses**

The Company allocates to the Divisions functional support costs that are considered to be directly or closely related to segment activity. Those allocated costs are included in the measurement of Division operating income. Other companies may charge more or less of functional support costs to their segments, and our results therefore may not be comparable to similarly titled measures used by other companies. The unallocated costs primarily consist of the buildings used for the Company's corporate headquarters and personnel not directly supporting the Divisions, including certain executive, finance, audit and similar functions. Unallocated costs also include certain pension expense or credit related to the frozen OfficeMax pension and other benefit plans.

Unallocated costs were \$34 million and \$33 million in the second quarter of 2015 and 2014, respectively, and \$55 million and \$59 million in the first half of 2015 and 2014, respectively. The decrease in the first half of 2015 compared to the same period in 2014 primarily resulted from synergies achieved at the corporate functional level following the Merger.

**Other Income and Expense**

<i>(In millions)</i>	<b>Second Quarter</b>		<b>First Half</b>	
	<b>2015</b>	<b>2014</b>	<b>2015</b>	<b>2014</b>
Interest income	\$ 6	\$ 6	\$ 12	\$ 12
Interest expense	(23)	(16)	(48)	(41)
Other income (expense), net	1	(2)	2	(2)

Interest expense in the second quarter of 2014 included a \$9 million reversal of previously accrued interest expense on uncertain tax positions following resolution of the related matter. Also, the second quarter and first half of 2014 included interest expense on debt held by the joint venture in Mexico that was sold in August 2014.

Other income, net includes gains and losses related to foreign exchange transactions, investment results from deferred compensation plans and, in 2014, losses on sales of the Boise Cascade Company stock received by the Company following the Merger.

**Income Taxes**

For the second quarter of 2015, the effective tax rate was primarily impacted by valuation allowances, which limited the recognition of deferred tax benefits for pretax losses in certain tax jurisdictions while income tax expense was recognized in tax jurisdictions with pretax earnings. The effective tax rate was also impacted by nondeductible foreign interest and other nondeductible expenses. The increase in the effective tax rate for the second quarter and first half of 2015 from the same periods in 2014 is primarily attributable to the release of valuation allowance in certain foreign jurisdictions and favorable settlements with certain tax authorities during the second quarter of 2014, which resulted in income tax benefits of \$4 million and \$3 million, respectively. In addition, the effective tax rate for the first half of 2015 reflects \$3 million of income tax expense related to the establishment of valuation allowance in certain foreign jurisdictions, as described below.

Following the recognition of significant valuation allowances in the U.S. and certain foreign jurisdictions in 2009, we have regularly experienced substantial volatility in our effective tax rate in interim periods and across years. Because deferred income tax benefits cannot be recognized in several jurisdictions, changes in the amount, mix, and timing of pretax earnings among jurisdictions can have a significant impact on the overall effective tax rate. This interim and full-year volatility is likely to continue in future periods until the valuation allowances can be released.

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The Company has significant deferred tax assets in the U.S. and in certain foreign jurisdictions against which valuation allowances have been established to reduce such deferred tax assets to the amount that is more likely than not to be realized. During the first quarter of 2015, the Company recognized income tax expense of \$3 million associated with the establishment of valuation allowances in certain foreign jurisdictions because the realizability of the related deferred tax assets was no longer more likely than not. As of the second quarter of 2015, valuation allowances remain in the U.S. and certain foreign jurisdictions where the Company believes it is necessary to see further positive evidence, such as sustained achievement of cumulative profits, before these valuation allowances can be released. The Company will continue to assess the realizability of its deferred tax assets.

During the second quarter of 2015, the Company received notification that the Internal Revenue Service ( IRS ) had completed its examination of the 2013 U.S. federal income tax return with no changes. Due to the completion of this examination, the Company decreased its unrecognized tax benefits by \$4 million during the second quarter of 2015, which did not impact income tax expense due to an offsetting change in valuation allowance. As of the second quarter of 2015, the Company's balance of unrecognized tax benefits is \$19 million, \$6 million of which would affect the effective tax rate if recognized. It is reasonably possible that certain tax positions will be resolved within the next 12 months, which would decrease the Company's unrecognized tax benefits by \$5 million but would not affect the effective tax rate due to an offsetting change in valuation allowance. Additionally, the Company anticipates 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 be reasonably made.

**NEW ACCOUNTING STANDARDS**

In May 2014, the Financial Accounting Standards Board ( FASB ) issued an accounting standards update that will supersede most current revenue recognition guidance and modify the accounting for certain costs associated with revenue generation. The core principle of this guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The guidance provides a number of steps to apply to achieve that principle. The standard is effective for the Company's first quarter of 2017. Early adoption is not permitted. Implementation may be either through retrospective application to each period from the first quarter of 2015 or with a cumulative effect adjustment upon adoption in 2017. Additional disclosures will also be required under the new standard. In July 2015, the FASB approved a one year extension to the required implementation date but also permits companies to adopt the standard at the original effective date of 2017. The Company is assessing what impacts this new standard will have on its Consolidated Financial Statements.

In April 2015, the FASB issued a new standard that will require debt issuance costs to be presented as a reduction of the related liability rather than as an asset. The standard is effective for the Company's first quarter of 2016 and will require prior periods to be adjusted. Early adoption is allowed. As of June 27, 2015, deferred costs of \$4 million relate to the Senior Secured Notes and will be reclassified in 2016 to reduce the carrying value of the debt and \$7 million relates to the Amended Credit Facility which has no outstanding borrowings and the debt issuance costs will remain classified as an asset.

In April 2015, the FASB issued a new standard that will allow companies a choice between measuring pension plan assets and liabilities based on the calendar year end date or, for companies with alternative year end dates (e.g., 52-53 week fiscal year), measurement closest to the calendar end date. The choice must be applied to all of a company's pension plans. It is effective for the Company in the first quarter of 2016; early adoption is allowed. The Company is evaluating this measurement option.



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**LIQUIDITY AND CAPITAL RESOURCES**

At June 27, 2015, we had \$867 million in cash and equivalents and another \$1.2 billion available under the Amended Credit Facility (as defined in Note 5 of the Condensed Consolidated Financial Statements) based on the June borrowing base certificate, for a total liquidity of approximately \$2.0 billion. We currently believe that our cash on hand, availability of funds under the Amended Credit Facility, and full year cash flows generated from operations will be sufficient to fund our working capital, capital expenditure and debt repayment requirements for at least the next twelve months.

At June 27, 2015, no amounts were drawn under the Amended Credit Agreement. There were letters of credit outstanding under the Amended Credit Agreement at the end of the second quarter of 2015 totaling \$91 million.

We also had short-term borrowings of \$6 million at June 27, 2015, under a local currency credit facility for our international subsidiaries that had an effective interest rate at the end of the second quarter of approximately 5%. The maximum month end amount occurred in June at approximately \$6 million and the maximum monthly average amount occurred in June at approximately \$5 million. These short-term borrowings represent outstanding balances on uncommitted lines of credit, which do not contain financial covenants.

The Company was in compliance with all applicable financial covenants at June 27, 2015.

Since the Merger date, we have incurred significant expenses associated with the Merger and integration actions, including costs associated with the Real Estate Strategy, and we have incurred significant expenses from restructuring activities in Europe. Approximately \$250 million of Merger integration costs are anticipated for fiscal years 2015 and 2016, including expenses related to optimizing the US retail store portfolio. International restructuring expenses are expected to be approximately \$80 million in 2015, consisting of severance and other employee termination benefits, as well as lease obligations and other costs.

For the full year 2015, the Company expects capital expenditures to be approximately \$200 million, including approximately \$80 million related to Merger integration. An additional \$80 million of Merger integration capital spending is anticipated for 2016.

We have entered into the Staples Merger Agreement with Staples and have agreed to pay a fee of \$185 million to Staples if the Staples Merger Agreement is terminated under any of the following circumstances:

the Company's Board makes a change in recommendation;

the Company terminates, at any time prior to obtaining approval of the Staples Acquisition from its stockholders (stockholder approval was received at the Company's Annual Meeting of Stockholders held on June 19, 2015), for the purpose of entering into an agreement for a superior proposal; or

the Staples Acquisition is not consummated by November 4, 2015 (or, February 4, 2016, if extended as permitted in the Staples Merger Agreement) or the Company's stockholders fail to adopt the Merger Agreement and to approve the Staples Acquisition (stockholder approval was received at the Company's Annual Meeting of Stockholders held on June 19, 2015), in each case, only if (i) a third party has made an acquisition proposal

before the Company's meeting of stockholders to vote on the Staples Acquisition and (ii) within 12 months of the termination of the Staples Merger Agreement, the Company enters into an alternative transaction. In addition, whether or not the Staples Acquisition is completed, the uncertainty related to the proposed Staples Acquisition could adversely impact our business through several factors, including, but not limited to: (i) our current clients may experience uncertainty associated with the Staples Acquisition and may attempt to negotiate changes in existing business relationships or consider entering into business relationships with parties other than us; (ii) we may face additional challenges in competing for new and renewal business; (iii) vendors or suppliers may seek to modify or terminate their business relationships with us; and (iv) our ability to retain and hire associates.

The Company currently estimates it will incur approximately \$100 million of expenses related to the pending acquisition by Staples, primarily employee retention costs and advisory fees, including \$49 million recognized in the first half of 2015.

**Table of Contents***Cash Flows*

Cash used in operating, investing and financing activities is summarized as follows:

<i>(In millions)</i>	<b>First Half</b>	
	<b>2015</b>	<b>2014</b>
Operating activities	\$ (135)	\$ (162)
Investing activities	(39)	(15)
Financing activities	(9)	(9)

*Operating Activities*

During the first half of 2015, cash used in operating activities was \$135 million, compared to a use of cash of \$162 million during the same period last year. Operating activities reflect outflows related to Merger and integration activities in 2015 and 2014.

Changes in net working capital and other operating activities in the second quarter of 2015 resulted in a \$311 million use of cash compared to a use of \$126 million in the first half of 2014. The 2015 use of cash in operating activities included \$77 million payment of the legal Settlement Amount and certain of the related fees. The remaining increased use of cash in the 2015 reflects a greater decrease in payroll and benefits consistent with settlement of higher accrued incentive pay and a greater decrease in rent and rent-related liabilities associated to store closures. Working capital is influenced by a number of factors including period end sales, 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, refer to Note 1 of the Condensed Consolidated Financial Statements.

The Company expects total Company sales in 2015 to be lower than 2014, primarily due to its decision to close certain stores, negative impact of currency translation, business disruption from the announcement of the pending acquisition by Staples, and continued challenging market conditions.

*Investing Activities*

Cash used in investing activities was \$39 million in the first half of 2015, compared to use of cash of \$15 million in the same period last year. During the first half of 2015, \$71 million was used for capital expenditures and \$10 million was used for acquisition of an interior furniture business. The acquisition is subject to a working capital adjustment which is expected to be completed during the third quarter of 2015. These outflows were partially offset by \$42 million of proceeds from the disposition of assets, primarily, the sale of a warehouse that was classified as held for sale at December 27, 2014. The first half of 2014 includes \$43 million proceeds from the disposition of Boise Cascade Company common stock received from the Boise Cascade Holdings distribution, offset by capital expenditures of \$66 million. The 2014 period also includes \$8 million from proceeds from assets sold.

*Financing Activities*

Cash used in financing activities was \$9 million in the first half of 2015 and 2014. During the first half of 2015, net payments on long- and short term borrowings were \$12 million compared to net payments of \$10 million in the same period last year. Employee share-based transactions resulted in a \$4 million and \$1 million source of cash in the first half of 2015 and 2014, respectively.

Under the Staples Merger Agreement, the Senior Secured Notes will be discharged, redeemed or defeased at the Effective Time of the Staples Acquisition. The discharge funding is anticipated to be part of the total Staples Acquisition consideration as part of closing.

### **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 2014 Form 10-K, in Note 1 of the Notes to the Consolidated Financial Statements and the Critical Accounting Policies and Estimates section of the Management's Discussion and Analysis of Financial Condition and Results of Operations.



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**Item 3. Quantitative and Qualitative Disclosures About Market Risk.**

At June 27, 2015, there had not been a material change in the interest rate, foreign exchange, and commodities risks 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 the Company's 2014 Form 10-K.

Changes in foreign exchange rates have affected comparison of reported U.S. dollars Division results. Where applicable, changes in U.S. dollars and constant currencies have been reported in Management's Discussion and Analysis of Financial Condition and Results of Operations.

**Item 4. Controls and Procedures.**

***Evaluation of disclosure 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 our management, including our 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. Each reporting period, the Company carries out an evaluation, with the participation of its Chief Executive Officer (CEO), and Chief Financial Officer (CFO), of the effectiveness of the design and operation of the Company's disclosure controls and procedures as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act.

Based on management's evaluation, as of June 27, 2015, the Company's CEO and CFO concluded that the Company's disclosure controls and procedures 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 fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

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**Table of Contents****PART II. OTHER INFORMATION****Item 1. Legal Proceedings.**

The Company is involved in litigation arising in the normal course of 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), the Company does not believe that contingent liabilities related to these matters (including the matters discussed below), either individually or in the aggregate, will materially affect the Company's financial position, results of operations or cash flows.

On February 4, 2015, Staples and Office Depot entered into the Staples Merger Agreement under which the companies would combine in a stock and cash transaction. On February 9, 2015, a putative class action lawsuit was filed by purported Office Depot shareholders in the Court of Chancery of the State of Delaware ( Court ) challenging the transaction and alleging that the defendant companies Office Depot, Staples, Merger Sub, and Starboard Value LP and individual members of Office Depot's Board of Directors violated applicable laws by breaching their fiduciary duties and/or aiding and abetting such breaches. The plaintiffs in David Raul, v. Office Depot, Inc. et al. seek, among other things, injunctive relief and rescission, as well as fees and costs. Subsequently, eight other lawsuits were filed in the Court of Chancery of the State of Delaware making similar allegations, namely Beth Koeneker v. Office Depot, Inc. et al., Jamison Miller v. Office Depot, Inc. et al., Eric R. Gilbert v. Office Depot, Inc. et al., The Feivel and Helene Gottlieb Defined Benefit Pension Plan v. Office Depot, et al., Charles Miller v. Smith et al., David Max v. Office Depot, Inc. et al., Patrick Connors v. Office Depot, Inc. and Steve Renous v. Smith et al. The Court subsequently consolidated all of the Delaware cases and named Jamison Miller and Steve Renous as co-plaintiffs and ordered the plaintiffs to file an amended consolidated complaint. The consolidated case is named In re Office Depot, Inc. Stockholders Litigation Consolidated, C.A. No. 10655-CB. After limited discovery, the plaintiffs and defendants agreed on certain additional disclosures to the Company's definitive proxy statement filed on May 18, 2015, which were made in an 8-K filing on June 5, 2015, and the plaintiffs withdrew from the calendar their planned motion to preliminarily enjoin the stockholder vote on the merger. The parties have agreed that the defendants need not respond to the current complaint. Additionally, in February 2015, two lawsuits were filed in Palm Beach County Circuit Court, namely Keny Petit-Frere v. Office Depot, Inc., et al. and John Sweatman v. Office Depot, Inc., et al. making the same allegations as in the Delaware actions. The lawsuits generally sought injunctive relief enjoining the consummation of the transaction, rescission of the transaction in the event it is consummated, damages, fees, costs, and other remedies. Office Depot filed a motion to dismiss the Florida lawsuits for improper venue, and that motion was granted on May 15, 2015.

In addition, in the ordinary course of business, sales to and transactions with government customers may be subject to lawsuits, investigations, audits and review by governmental authorities and regulatory agencies, with which the Company cooperates. Many of these lawsuits, investigations, audits and reviews are resolved without material impact to the Company. While claims in these matters may at times assert large demands, the Company does not believe that contingent liabilities related to these matters, either individually or in the aggregate, will materially affect its financial position, results of operations or cash flows. In addition to the foregoing in 2009, State of California et al., ex rel. David Sherwin v. Office Depot, Inc. (the Sherwin lawsuit ) was filed in Superior Court for the State of California, Los Angeles County, and unsealed on October 16, 2012. The lawsuit asserted claims, including claims under the California False Claims Act, based on allegations regarding certain pricing practices under now expired agreements that were in place between 2001 and January 1, 2011, pursuant to which governmental agencies purchased office supplies from us. The plaintiffs sought monetary damages and other relief, including trebling of damages and statutory penalties. On June 25, 2014, the Company participated in a non-binding, voluntary mediation in which the Company negotiated a potential settlement to resolve the matter. During the second quarter of 2014, the Company recorded an \$80 million incremental increase to the legal accrual which included the potential settlement, as well as attorneys' fees

and other related legal matters. On December 19, 2014, Office Depot and the plaintiffs executed a Settlement Agreement to resolve the lawsuit. Pursuant to the terms of the Settlement Agreement, the Company agreed to pay the plaintiffs \$68 million to settle the matter (the Settlement Amount), as well as \$9 million in legal fees, costs, and expenses. In exchange for, and in consideration of, the Company's agreement to pay the Settlement Amount, the plaintiffs agreed to dismiss their action against the Company with prejudice. In February 2015, the court entered orders approving the settlement and dismissing the case with prejudice. The Settlement Amount was subsequently placed in escrow pursuant to the Settlement Agreement and, during the second quarter of 2015, was released from escrow and disbursed in accordance with the terms of the court's orders.

In addition to the foregoing, *Heitzenrater v. OfficeMax North America, Inc., et al.* was filed in the United States District Court for the Western District of New York in September 2012 as a putative class action alleging violations of the Fair Labor Standards Act and New York Labor Law. The complaint alleges that OfficeMax misclassified its assistant store managers (ASMs) as exempt employees. The Company believes that adequate provisions have been made for probable losses and such amounts are not material. However, in light of the early stage of the case and the inherent uncertainty of litigation, the Company is unable to estimate a reasonably possible range of loss in the matter. OfficeMax intends to vigorously defend itself in this lawsuit. Further, *Kyle Rivet v. Office Depot, Inc., formerly known as Constance Gibbons v. Office Depot, Inc.*, a putative class action that was instituted in May 2012, is pending in the United States District Court for the District of New Jersey. The complaint alleges that Office Depot's use of the fluctuating workweek (FWW) method of pay was unlawful because Office Depot failed to pay a fixed weekly salary and failed to provide its ASMs with a clear and mutual understanding notification that they would receive a fixed weekly salary for all hours worked. The plaintiffs in both complaints seek unpaid overtime, punitive damages, and attorneys' fees. The Company believes in this case that adequate provisions have been made for probable losses and such amounts are not material. However, in light of the early stage of the case and the inherent uncertainty of litigation, the Company is unable to estimate a reasonably possible range of loss in these matters. Office Depot intends to vigorously defend itself in these lawsuits.

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OfficeMax is named a defendant in a number of lawsuits, claims, and proceedings arising out of the operation of certain paper and forest products assets prior to those assets being sold in 2004, for which OfficeMax agreed to retain responsibility. Also, as part of that sale, OfficeMax agreed to retain responsibility for all pending or threatened proceedings and future proceedings alleging asbestos-related injuries arising out of the operation of the paper and forest products assets prior to the closing of the sale. The Company has made provision for losses with respect to the pending proceedings. Additionally, as of June 27, 2015, our estimate of the range of reasonably possible losses for environmental liabilities with respect to certain sites where hazardous substances or other contaminants are or may be located was approximately \$10 million to \$25 million. The Company regularly monitors its estimated exposure to these liabilities. As additional information becomes known, these estimates may change, however, the Company does not believe any of these OfficeMax retained proceedings are material to the Company's business.

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

At June 27, 2015, pursuant to an indenture, dated as of March 14, 2012, we have restrictions on the amount of cash dividends we can pay. We have never declared or paid cash dividends on our common stock and do not anticipate declaring or paying any cash dividends on our common stock in the foreseeable future.

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**Item 6. Exhibits.**

Exhibits

10.1	Office Depot Corporate Annual Bonus Plan (Incorporated by reference from Office Depot, Inc.'s Current Report on Form 8-K, filed with the SEC on June 22, 2015).
10.2	Form of Agreement For Cash Settled Short-Term Performance Award For Executive Officers
10.3	Office Depot, Inc. 2015 Long-Term Incentive Plan (Incorporated by reference from Office Depot, Inc.'s Registration Statement on Form S-8, filed with the SEC on June 19, 2015).
10.4	Form of 2015 Restricted Stock Award Agreement (Incorporated by reference from Office Depot, Inc.'s Registration Statement on Form S-8, filed with the SEC on June 19, 2015).
10.5	Form of 2015 Restricted Stock Unit Award Agreement (Incorporated by reference from Office Depot, Inc.'s Registration Statement on Form S-8, filed with the SEC on June 19, 2015).
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 Schema Document
(101.CAL)	XBRL Taxonomy Extension Calculation Linkbase Document
(101.DEF)	XBRL Taxonomy Extension Definition Linkbase Document
(101.LAB)	XBRL Taxonomy Extension Label Linkbase Document
(101.PRE)	XBRL Taxonomy Extension Presentation Linkbase Document

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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: August 4, 2015

By: /s/ Roland C. Smith  
Roland C. Smith  
Chief Executive Officer and  
Chairman, Board of Directors  
(Principal Executive Officer)

Date: August 4, 2015

By: /s/ Stephen E. Hare  
Stephen E. Hare  
Executive Vice President and  
Chief Financial Officer  
(Principal Financial Officer)

Date: August 4, 2015

By: /s/ Kim Moehler  
Kim Moehler  
Senior Vice President  
and Chief Accounting Officer  
(Principal Accounting Officer)