Glass Lewis Proxy Talk

Office Depot Proxy Contest with Management and Directors

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OPERATOR: Good day, ladies and gentlemen, and welcome to the Glass Lewis Proxy Talk Conference call. All lines have been placed on a listen only mode for this call. Institutional investors that would like to ask questions of the participants may do so by e-mailing them to proxytalk@glasslewis.com.

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As a reminder, this conference call is being recorded.

At this time, it is my pleasure to turn the call over to our host, Warren Chen, managing director, mergers and acquisition research at Glass Lewis and Company.

WARREN CHEN, MANAGING DIRECTOR, MERGERS AND ACQUISITION RESEARCH, GLASS LEWIS: Thank you very much. Hello, everyone, and welcome to Proxy Talk. This call today will be discussing the proxy contest at Office Depot. A dissident shareholder, Woodbridge Capital, which owns about 1.1 percent of Office Depot, is seeking to convince fellow shareholders to elect two of its director nominees in place of Mr. Odland and Mr. Fuente.

Joining me on the call today are representatives of Office Depot. And we have Mr. Steve Odland, chairman and CEO; Mr. Charles Brown, president, international and acting CFO; Mr. Chuck Rubin, president, North American retail; Mr. Steve Schmidt, president, North American business solutions; Neil Austrian, director; and Mr. Lee Ault, director.

And I just want to provide a little bit of background before we hear from the gentlemen from Office Depot. Office Depot believes that the incumbent board and management are well qualified- they're in the best position to lead the company. And Office Depot believes that the current turn around plan has shown positive results in that Mr. Levan and his nominees have questionable track records, just by way of background.

And a meeting is scheduled for April 23rd and bear in mind that if you have any questions today regarding the call, please e-mail them to us at proxytalk@glasslewis.com and we'll work them in during the Q&A session.

So at this point, I'd like to offer an opportunity for the gentlemen from Office Depot to provide some background on a contest and their point of view in terms of why shareholders should reject the Woodbridge nominees.

Gentlemen, the floor is yours.

STEVE ODLAND, CHAIRMAN, CEO, OFFICE DEPOT: Good morning. Thanks very much. This is Steve Odland, CEO of Office Depot and Warren has introduced the other participants today. Lee Ault is with us, who is a long term board member of Office Depot and is the chairman of our compensation committee. Neil Austrian also is with us. Neil is the chairman of our nominating corporate governance committee and as well serves as lead director for our board.

Office Depot, I think, as most people know is a nearly $16 billion company. It's the most global of the office products providers, doing business in 43 countries today. Forty-four percent of our business is retail in North America that was our core, of course. But it is the smallest portion of our business today.

The larger portion is our delivery business broken out into North American Business Solutions, which is nearly 30 percent of sales. And then our international business, which does have all channels, but mostly in the delivery business and that's also in the high 20 percent of sales.

I think it's important to understand how Office Depot came together. We're only a 21 year old company. It's been an American success story with the founding – with one store in Florida in 1986 and today in the 43 countries and nearly $16 billion.

But we've come together over the years into a whole variety of mergers and acquisitions that set the stage for the size and scale of the business. Nearly 30 percent of our business in North America today is concentrate in two states, Florida and California. That's because we started in Florida.

We made an early acquisition of a company named – called Office Club, which was a California company. And then we made acquisitions of contract stationers, which were largely in California and as well Viking Office Products, which had a heavy business in California.

So, over the years we've developed and we have an overweighed amount of business in those geographies. We also grew and developed very rapidly and we found ourselves in the situations several years ago where we did have non-integrated acquisitions. We were at end-of-life on our IT systems and lots of challenges for us.

Neil, I think, maybe it would make the most sense if you could just say a few words about the situation that the board faced in 2004 and some of the issues and how you went about making the decisions that the board made.

NEIL AUSTRIAN, DIRECTOR, OFFICE DEPOT: Thanks, Steve. I became the interim chairman and CEO in October 2004 when the board became convinced that we had to make a management change. And some of the thinking at that time was that we had a functionally aligned organization that was a matrix management and the board really felt that that needed to be changed in terms of divisional profit responsibility.

We had made two major acquisitions, Viking in 1998 and Guilbert in 2003, which hadn't been integrated as fully as expected. And when you look at their different IT platforms, Office Depot was on a legacy system, G.D. Edwards was on a Viking system, Guilbert was on a SAP system. So there really had to be a total rethinking of the IT system to get us all on a common platform.

At the time, we had a duplicate supply chain in terms of the way the business was run. Our operating margins versus our competitors, particularly Staples, had not gotten to a point that the board was satisfied with. And it was a real inconsistency in the shopping experience because we had a large number of stores that were of different formats and different plan-a-grams. When the board conducted a search, we wanted a proven leader with a track record who had retail experience, high set of ethical values, someone with a proven turn-around ability and a clear track record in his ability to build and hold a management team together. And we unanimously settled on Steve Odland.

Steve joined the company in March 2005, I'll come back to these set of issues at the end and talk about how the board perceives we've done against them.

ODLAND: So, we set out in 2005, with a high level of urgency to turn around the business. First thing we did was create three divisions and we promoted Chuck Rubin, who has 27 years of retail experience, almost all in merchandising, but also store operations and marketing to run our retail business.

We recruited Steve Schmidt last year to be president of our business solutions division. And we promoted Charlie Brown to be president of international. Our – I won't go into detail about the plan that we put into place.

We can do that through the questions, but Chuck Rubin, a career retailer, put 14 straight quarters of record growth on the board. We had tremendous growth in our contract business and North American Business Solutions. And Charlie Brown has led the business for eight consecutive quarters in local currency growth.

We also have delivered $600 million worth of cost reductions by taking waste out of the business. And the impact from the turnaround was phenomenal. From 2004, through the first half of 2007, we had record sales; we had record earnings; we had record margins; and our stock price grew 81 percent after we delivered $2 billion of capital to our shareholders, which is 140 percent of our after tax earnings.

So, last year, first half of last year, we had a tremendous success in all-time high record earnings and profitability. We have been impacted as almost every business in America has been impacted by economic conditions. Remember, I said that 30 percent of our business is concentrated in two states that have been the hardest hit.

I think anybody who does business in Florida has been hit and certainly should understand the situation when you have an over concentration of business in those two markets. Clearly we'd like to have more geographic dispersion, but we will do that over time.

So, 2007 became a story of two halves. All time record high performance in the first half. But a significant slow down in the second half. That significant slow down has been experienced throughout the industry. Our top store sales were identical to Staples in the fourth quarter. And so the top line performance has been the same.

Just a couple more points before we turn it open for questions. We recognized the slow down immediately last summer. We developed a new plan, which is highly focused on dealing with our customers and taking care of business in this environment. The plan was developed; reviewed with the board; the board had significant input in October.

In November, we took it to our shareholders and we met with shareholders as we do regularly. And we visited shareholders accounting for over half of our outstanding shares. We went through that turn-around plan with our shareholders and explained our situation and got their input into this. So this is a plan that has significant number of metrics behind it. Has details on every strategy behind it.

Now, we put some of the plan summary on our website to share it with people. Clearly, there are details behind that and metrics behind that that we obviously don't post for our competitors to see. But that is a plan that we are executing today and we believe will be very, very productive.

Let me stop there and open it up to questions and we can talk about, you know, issues related to the plan, the board, experience and so forth. Warren?

CHEN: OK, thank you. Let's start off by asking, you also mentioned a little bit about in your opening talk here, Office Depot's performance in the past few years. How do you explain the dramatic stock price drops and since mid-'07 most recent period and how do you think shareholders should look at it and do you think shareholders should be concerned about it?

ODLAND: Well let me say, first of all, that management is not happy with where our stock price is. We're not happy with where our performance is currently. The board is not happy and I would doubt that any shareholder who's been a shareholder for the long term is happy at all.

And we recognize that which is why we have developed the strategic plan and sought their input into this. But the fact of the matter is we had a first half of last year that was an all time record high. We're lapping that currently. But we have felt the slow down.

Our business, at retail as well as in our contract and in our catalog business is predominately 'B' to 'B'. Even in the stores, which some people think of as a consumer business, it's not a consumer business. We don't run it that way. Two-thirds of the business in the stores is sold to very small businesses which we call micro businesses, under 10 employees.

See, our customers are hurting, especially in the markets in Florida and California. Our customers have gone out of business. They've had lines of credit dry up. They haven't been able to expand. They've been cutting back on their employment.

We supply the back office and the supplies that drive these businesses. When their businesses dry up, they are unable to buy from us because they don't have the usage of office products and services. Clearly, we are not happy with that situation.

But we, you know, we don't use the economy as an excuse, but we share the analytics that we have experienced with our business so that people understand factually what is going on. More importantly, we've shared very detailed plans with our shareholders and we've been implementing those plans since November in order to adjust our business to the economic situations that our customers are facing.

UNIDENTIFIED PARTICIPANT: The thing is we got ahead of ourselves too.

CHEN: Then is there evidence that the new plan is succeeding?

ODLAND: We believe it is. We, of course, we're not at all happy with our performance in the fourth quarter. But during our fourth quarter call, we pointed out and we took people through the plan, but we also have committed to improving our margins sequentially in the first quarter by several hundred basis points. We have metrics behind that.

In the first half we said that since we're lacking all time record highs last year, we will be down in earnings per share in the first half, but that sequentially we will make improvements in our margins and we will begin lapping our own performance towards the end of the year so we will see improved performance year over year by the end of this year.

AUSTRIAN: This is Neil Austrian, you know, basically if you look at the business when Steve came in and you look at the stock price, he did an extraordinary job and all the media and all of the industry publications touted a great change in the company.

2005, 2006, first half of 2007, the stock probably got ahead of itself at that point in time. But clearly there was an awful lot of money made in this stock since Steve got here. We also returned over $2 billion in cash through stock repurchases to stockholders.

So all of a sudden we've got a 2.5 year performance that both Wall Street, our stockholders, the board, viewed as a pretty good performance and we've had the last six or seven months of what nobody's happy with. No one's happy with the stock price, but I think you have to have an understanding of the environment that you're dealing in and where we can leverage the business.

CHEN: And, in terms of turn-around plans and that's been executing since late last year, you know, is there a dramatic difference in this plan than other efforts sort of been placed before by management? And how much time are you asking shareholders to see any turn around?

ODLAND: The plan is different. Obviously, it had to be rewritten given the macro environment that we face and all businesses face today. Chuck, do you want to talk – give a few highlights of the North American Retail Plan?

CHUCK RUBIN, PRESIDENT, NORTH AMERICAN RETAIL, OFFICE DEPOT: Yes, that will be fine. Just to reinforce some points that Steve mentioned earlier, I have 27 years of experience, all dedicated to merchandising, marketing and store preparations. Six of those were with Accenture, a worldwide consulting firm. The rest of them and where I dedicated only on – focused only on retail operations in merchandising and marketing issues in large companies, large retailers. The balance in industry.

The focus that we have in retail is building on the leading technology and furniture business that was established over the past couple of years. We're focused in 2008 on a number of factors; they boil into three big buckets. One is adding value to our assortments, especially within our supply's assortment. To address the needs of those micro business customers in today's environment.

This includes smaller pack sizes; lower price points; bonus packs. It also includes leveraging the floor space in our stores better than we do today in high traffic areas. All of these things are in place and we'll be building upon them as the year unfolds.

The second big area is in our loyalty program. We have an award winning leading – industry leading program that is the best benefit program for these micro customers. It includes money back that we provide to them. That's especially focused on the supply piece of the business. Also affinity programs with third parties on airlines and hotels and car rentals, things that these micro customers need to help them in today's day and age.

And then lastly, through a banking relationship that we have, we offer extended financing. Which we also think is important for these loyal customers. We're anxious to continue to add to our base of customers, which we've been doing successfully. And we're aiming to increase our share of wallet with them as well.

The third big bucket is adding our service business to complement our product business. This includes our copy business which is essentially a full service marketing arm for these micro customers as well as our technology services business to install, upgrade, repair computers, home networks, office networks, television installation, et cetera.

Both of those service businesses will be complemented by others that we'll introduce this year. And they're also high margins, but they also compliment the product offering that we've built. So that's what we're focused on right now.

ODLAND: And that's a very high level. Obviously there's an incredible amount of detail and metrics behind it.

Warren, if you wouldn't mind, if we could just go through a couple points each on the other divisions, I think it would be helpful for our listeners. Steve Schmidt, if you could just highlight from North American BSD.

UNIDENTIFIED PARTICIPANT: And your business experience.

STEVE SCHMIDT, PRESIDENT, NORTH AMERICAN BUSINESS SOLUTIONS DIVISION, OFFICE DEPOT: Yes, Steve, thank you. First of all, my background, you know, 30 years in the business. About 18 years in the consumer package goods industry. And the last 12 years at ACNielsen where I ran the U.S., ran North American, the Americas and then was president and CEO for the last five years. So I brought really extensive 'B' to 'B' background and experience to a 'B' to 'B' job here at Office Depot.

The four major thrushes that we're focused on in the 'B' to 'B' space, and let me start with the large contract side of the business. Today the mix of our business is two-thirds large, one-third small to medium. Our large contract business where we've been gaining share, however gaining share at reduced margins in a very competitive environment.

And so we have undertaken a restructuring of our strategy with our large contract customers. Identified profitability and segmentation by channel, legal, financial, healthcare, et cetera. We've established new financial metrics in addition to working with our core base of customers to remix the product lines in order to improve the profitability of this important sector which we continue to grow.

The second big area of opportunity is the small to medium size customer segment. And we have launched what we're calling a contact strategy. Two major elements to this. First of all, detailing exactly how we want to contact every one of our customers.

We contact them today through catalogue, online, face to face, e-mails, et cetera, developing an optimum contact strategy as well as understanding the cost to serve. And then putting on top of that a share of wallet model whereby we can identify what they spend in total office supplies; compare that to their spending with us; and then do a share of wallet analysis.

We are actually testing that right now and will be rolling this out nationally through Q2 and Q3 to focus on that very important small to medium size customer segment. What we recognize is that in that small to medium customer segment, you make anywhere from eight to 12 points of higher margin than you do on the large contract side. And it's an important growth area for us.

The third major focus is direct marketing. An area where we really had a gap in terms of expertise. I brought in a whole new management team in the direct marketing area because we needed to really refocus our efforts as it related to catalogue, online and then TAM.

On the catalogue side, we have changed our strategy. We have, and this involves everything from our distribution strategy to pagination, the way that we look at each page within a catalogue and how we think about up-sell, graphics, et cetera, and applying that same strategy to online.

And the other area is TAM, which is our telephone account management business. This focuses on our smallest customers, one to 10, white collar workers. Here we basically have reinvented the strategy as it relates as to how we attack this particular segment.

We've introduced new marketing strategies. Key performance indicators, as well as hiring standards. And we've begun to see this business move into the correct direction as we go forward. And then finally, wrapping all that around people and making sure that we have a world class selling organization to drive the business forward.

ODLAND: OK, why don't we stop there Warren and we can go into international if there's a question on it.

CHEN: OK, let's stay on performance for a little bit. In the distance, compare your performance with – against that of the Staples. So from your perspective, do you think that's a right company to compare yourself to?

ODLAND: Well, I think you have to look at the competition that we face today and it's a lot different than 10 years ago. Our leading competitors are Wal-Mart, Costco, Sam's Club and so forth. If you look at Staples, Office Max and Office Depot combined, we have less than 10 percent of the entire market.

So when you think about competition you have to think about all the competitors but also the channels, the internet has become an immense source of competition for us. And we're one of the leading internet retailers today with about $5 billion worth of internet sales that has been developed in the last half a dozen years or so.

But clearly, Staples and Office Max are good competitors of ours. They are different than us though and I think it's important to understand the geographic mix difference. While we have 30 percent of our sales in – concentrated in two states, Florida and California, largely because of our legacy, Staples have a large amount of business in Canada. They pretty much own Canada and in the Northeast. And so you'll see differences in performance based on the geographic concentrations.

So too, Staples for example, has a much bigger base of customers in the small business sector in their catalogue business, Quill and Staples catalogue business. And that's much higher margin business as Steve Schmidt just pointed out.

Steve, I don't know if you want to make any comments related to that?

SCHMIDT: Well I just think when you look at, on the BSD side of the fence when you compare us to Staples, you can actually explain the entire margin difference between our two businesses really based on mix, as Steve said.

We have two-thirds of our business in large, one-third in small to medium and theirs is exactly the opposite. Additionally, all the things that we're doing as relates to IT are things that Staples has already put in place. They've got in place a common ERP system; they've got all their customer data on one CRM tool. And all of these things will be – we're implementing as we move into 2008 which are at this point areas of opportunity for us also.

AUSTRIAN: I also might point out that when you look at the retail stores and you look at geographically where each of the three office superstores have their stores, Staples has a greater percentage of their stores in what we consider single markets, meaning they don't compete with Office Depot or Office Max. Where as we and Office Max have significantly more markets that are competitive.

CHEN: So, taking into consideration different customer mix, you know, geographic focus and the size perhaps, those areas, our difference, kind of limit your opportunities?

ODLAND: Well, we think we have tremendous opportunity for profitable growth in all three of our businesses. We haven't talked about international. But in North American retail, we think we can double the store count. In North American BSD, we only have about 3 percent market share in that business.

We think we've been gaining market share in the contract, large contract business as well as in the public sector and education sectors. We have lost some market share in the catalogue business and among very, very small businesses which is why Steve has reacted and put a new team in place. We're seeing better trends in the business today than we have, certainly, since I've been here.

Internationally, we think that there's a tremendous amount of growth potential for us, certainly in our existing markets, but also in emerging markets. We also think that there's 300 basis points worth of margin opportunity that we can create on top of all of that with certain projects that we have underway. And we've laid that out for our shareholders as well.

Those 300 basis points with a bottom line margin can be driven through the development – further development of our private brand and leveraging our direct import capabilities which we've just launched in Shenzhen, China. Centralization of country by country operation. In Japan, European operations are moving from duplicate supply chains to a single supply chain and we're moving there.

In North America, we have it all laid out and the first facility should open here at the beginning of 90 – of 2009. And then finally, our IT conversion, which we have spent two years developing and building and testing, which is – anybody's who's ever worked in implementation of IT knows it a very, very sensitive area and you've got to do it right. We're rolling out he first phase this summer. And it's all ready to go. And then, subsequent phases will follow.

So, all of that should provide 300 basis points worth of margin expansion on top of the growth opportunities that we've laid out.

UNIDENTIFIED PARTICIPANT: That's independent of whatever (INAUDIBLE).

ODLAND: OK?

CHEN: So, this question just came in and staying with the performance theme here, what are three key mistakes Office Depot makes communicating its '05 strategic plan?

ODLAND: Well, you know, I certainly, you know, we're a humble group. We know that at any point in time there's a hundred things that we could be doing better and you know we're working that everyday. And I think, you know, every business has got those things.

I think the plan has been very, very successful though and I think we have to point out that it's been record performance from 2004 through the first half of 2007. You know I think that we would have liked to have had better performance certainly in the Viking Office Depot catalogue transition.

That transition began in 2004 and we lost our direct marketing capability as the transition was executed in 2004. It has clearly been a challenge for us and we've clearly lost share there. We're not happy with that at all. And we're working on that.

We think that we could have moved faster to consolidate operations in Europe and internationally. But it takes time in Europe to work through the work council and Charles, maybe I could ask you to talk about those efforts because that's clearly something that you've been pushing urgently.

CHARLES BROWN, PRESIDENT, INTERNATIONAL, OFFICE DEPOT: Right. I think you have to go back to 2004, and we had just acquired the Guilbert business doubling our size in Europe and again that was public information. And, you know, we set up about half to consolidate that. It is very challenging because Europe has very extensive labor laws and the speed in which you can go – you have to, it's a very involved process.

But we made a lot of progress. We've gone from 36 warehouses at that point in time to; we're down to 21 now. We will be closing four more warehouses this year and ending up at about the 13 to 14 range for all of Western Europe. So that's a tremendous accomplishment.

We're also doing the same thing with call centers, where we had duplicated call centers. And something that we're very proud of is our opening of the shared service center in Eastern Europe where we take advantage of the labor arbitrage between Western and Eastern Europe.

We successfully moved the U.K. back office, its accounting function, to the center in the fourth quarter of last year. We're almost finished with moving the back office in the French business; we'll have all of Western Europe done by the end of this year. Again, lots of progress, but it is a lot of work.

ODLAND: I think, just to wrap up that question, speed is of the essence and I think if we could all wave a magic wand, we would have executed everything quicker. You know the IT systems have been a mess.

And we started urgently on that. But we do have it all built and tested and ready to go. We wish we had that in place. It would certainly, in our BSD business, we could use the CRM tools that our competitors have and we don't have. But those are some things that have frustrated us, Warren.

CHEN: OK. So, looking at the plans you have in place right now, how is that different than the business plan?

ODLAND: Well, I think as we've, Chuck, you may want to again talk through how the plans that we're implementing right now are different than what you set out to implement three years ago.

RUBIN: Well, three years ago we had a number of things that we needed to do around the stores themselves. Keep in mind that back in 2004, we had roughly 900 stores spread over close to 700 different formats. Not a very efficient or customer friendly way to run a store group. So we set out to develop and implement and roll out a new store format.

Better than half the chain is operating in that format today. It's gotten very good reviews from customers, the performance financially in the stores has been right on track with where we thought it would be. And the store management and the store crews liked the store because it's a more customer friendly and operationally a better store to run.

So that was a core component of what we were focused on a few years ago. We also were focused at the time on building some of the new technology businesses that the company wasn't strong in and have been successful in that.

With those two components well entrenched in implementation, the strategy that we're focused on right now is back to what my comments a few minutes ago, continuing to build our supplies business, our core supplies business, which is higher margin.

Continuing to build upon the loyalty program. We continue to add benefits for our customers in an attempt to build and attract new customers as well as expand the share wallet with out customers. We're laying a good foundation but we still have much room for improvement.

And then lastly on the service business, here again, we've laid a good foundation. Our copy business has been gaining share over the past year, but it's still a very young business with lots of upside. The same is true in technology services, high margin, lots of upside complements the product side of the business.

ODLAND: So, Chuck, I think the differences are we didn't have a format, a prototype that we were comfortable with three years ago. We now do. And we're rapidly revising all the stores to the MPU format. I think the difference is, whereas we were focused strictly on product four years ago, we're now launching services in the stores and I think you've got a greater focus on the operations within the store.

You might want to mention …

RUBIN: Yes, I…

ODLAND: …the great improvement in the customer service scores over the past three years.

RUBIN: You just took the words out of my mouth, Steve. Three years ago, three or four years ago, we raised the bar in terms of customer service in the stores.

I'd remind everybody that we use an independent, anonymous shopping service that visits every one of our stores a couple of times a month, with rotating shoppers so the store personnel don't know who's coming into shop. Three, four years ago, our service scores were in the 70's. Today they're in the 90's and have increased over the past couple of years. And we continue to be very focused on improving that even further.

CHEN: So, let's shift gear a little bit. So I understand earlier this year, state of Georgia terminated its contract with you guys. I think there's also currently an investigation going on in the state of California. Do you think that this is a signal to shareholders of deeper problems?

SCHMIDT: Yes, this is Steve Schmidt. First of all we service today at a service rate of over 99 percent in terms of our overall service satisfaction with our customers. As it relates to the government sector this is one – we are the largest player in the government sector.

And we have over 18 state contracts in this very important area. And its one of our key growth areas where we continue to satisfy our state government contracts. In the case of the state of Georgia, it's a contract that we just recently won.

We were awarded the contract in March of 2007, and to be blunt, the information that has been published by third party independent individuals is grossly overstated and inaccurate. We are working right now with the state of Georgia and will be continuing to discuss with them and when the facts come out there will be a different story told.

There is clearly a strong political agenda and this is one of the things everyone needs to understand when dealing with the state governments, there's both a business agenda and a political agenda. And there's a very strong political agenda here being supported by the independent office supply companies and we will continue to do what we believe is appropriate.

ODLAND: Steve, I think if we've been inaccurately accused of over billing. You might want to talk about, when some of the things happened during the transition and that point of view.

SCHMIDT: Yes, a couple other key points would be, first of all, the state of Georgia awarded a sole provider, sole source contract. That was their decision when they went through this RFP process. And they raised questions on pricing and you know there were certain accusations as it related to overpricing. In fact, we actually under-charged.

When A.T. Kearney who was an independent auditor, hired by the State of Georgia, the facts, as they come about, which we have presented to the State of Georgia, is that we actually under-charged. And in any case where we had over-charged, we had rectified that situation.

ODLAND: So, there's some pricing discrepancies in the change-over in the first few weeks of the contract net, net. It was an under-charge.

But this attack from the small office products dealers is continuing and they have taken the campaign now to California to try to spread misinformation there as well. And we're going through a complete audit at our request to go through and to verify and demonstrate that we have fulfilled all the contractual requests of the state of California. And our service levels are actually higher than their expectations.

CHEN: OK. So, let's take a look at the makeup of the board. You noted that half of the board joined in the last four years. Participants noted that you have five directors who have served over 10 years. So is it your opinion that there is no need to add or have some new directors and perhaps this is unneeded at this point?

AUSTRIAN: This is Neil Austrian, let me try and respond to that. We have 12 directors on the board. Eleven of the 12 are independent according to New York Stock Exchange guidelines. Three of the audit committee members qualify as financial experts.

As you correctly stated six of the 12 board members have joined within the last four years, two within the last two years. We think that 12 board members is a reasonable number. It enables us to handle the committee structure. I'll point out that last year; we had 39 board meetings and committee meetings among our board members. I'll point out that every board member attended every board meeting.

So at this point in time, we don't think we need to add to the board when you look at the experience on the board, if I stay for a minute with just retail experience. Dave Bernauer, former chairman and CEO of Walgreen's, with over 40 years of retailing experience. Dave Fuente ran the Sherwin and Williams paint stores. Was recruited when Office Depot had five or six stores. And really built Office Depot in the retail sector until he stepped down in 2001.

Myra Hart, who was one of the founders of Staples, teaches now at Harvard Business School, a former director of Star Markets and Raw Ahold. Kathleen Mason, who we added within the last two years, the current CEO of Tuesday Morning, former Chair and CEO of Cherry & Webb, currently a director of Genesco.

And Steve Odland, who spent quit a bit of time in the retail business with both the grocery chains, with AutoZone and now with Office Depot. I look at the other directors that we've got and four or five of us have had significant operating experience in running businesses, writing strategic plans. All of us, all of us serve on other public company boards.

So I look at our board today, and I think we've got an extremely qualified, capable, committed board. You look at the retail piece which I dwelt on; you have to recall today less than half of our business is retail, 44 percent. So besides retailing you clearly need some other experience on the board. And I think we've got both marketing experience and some very good financial experience. As well as international experience.

CHEN: All right. So I just – so, just a reminder, if you have any questions you would like to ask, please send them to proxytalk@glasslewis.com and we will address them.

Let's shift the focus to compensation. There's some concerns out there about, Steve, your compensation for '07 where it looks like there's a retention bonus of $10 million or roughly that value and at the same time the stock performance had done quite poorly. Should shareholders be concerned about that?

ODLAND: Well, on the line we have Lee Ault who is our chair of our compensation committee, Lee; would you like to address the compensation question?

LEE AULT, DIRECTOR, BOARD OF DIRECTORS, OFFICE DEPOT: Yes, I'd be pleased to. When you examine the record and the line pay for the appropriate year, you'll see that Office Depot has a total commitment to pay for performance and in practice executes that philosophy.

Which means that we pay more for good performance and less when performance falls short. And in this way, pay is directly tied to the interest of shareholders. Confusion can arise because we pay bonuses in February of the year following the year under review. And equity awards are made in February or March, which are in part tied to prior year performance as we explained in the proxy.

So you must take this into consideration to understand what we do. Steve Odland mentioned previously that for 2005, 2006 and for the first six months of 2007, Office Depot achieved outstanding results under his leadership. And the results turned down during the second half of '07 as the housing crisis set in and the retail industry came under severe pressure.

So, if you look at the actual compensation and you go by year, the – in 2006, which was an extraordinary year, and just to refresh your minds, it was a year when earnings per share grew from $1.41 to $1.90, that's a 35 percent increase, EBIT margin increase from 4.6 percent to 5.3 percent. And virtually all of the metrics showed significant improvement over prior years.

For that year, Steve received no salary increase. He received a cash bonus to reflect that superior performance, approximately – approximating approximately $2.2 million. And he received a $7 million long term equity award that was granted in February of 2007 that reflected peer group practice and industry practice as well as the excellent 2006 performance.

Then in 2007, last year, his compensation included no salary increase. There were zero bonuses, reflecting the performance levels which were below the goals and he received a $5 million long term equity award that was granted in February of this year that reflects peer group practice and the 2007 performance. So the equity award of the $5 million compares with the $7 million in the prior year.

Now, I want to talk a little bit about the special equity award that was made in 2007 and tell you about some of the factors that went into our thinking as we thought about the relative merits of making such an award. And we looked at the outstanding performance of the company through the time of the award in February 2007, or – when we considered this at the beginning of last year.

In the industry, there are many retail CEOs that were being changed out. Steve Odland was a hot commodity in the market place and risk existed that LDL and other firms might lure him away. And we felt strongly that Steve was the key to the realization of our long term goals and recognized that, you know, not only the performance of Office Depot, but the outstanding performance that he had at – in positions that he held prior to joining the company.

There was also a precedent for making such an awards and we spent a lot of time looking at what other companies had done to hold on to CEOs who were performing well. And we found that there were 18 retail companies that awarded special magna retention grants over a three year period that averaged $14 million. And that compares with the $10 million that Steve received. All of which had less performance requirements or certainly the lion's share of which had lesser performance requirements.

So here's what we did. Now this is lined out – outlined in the proxy, but I'd like to go over it. The special retention grant had a shoals, black shoals value of $10 million. One-half of it was in the form of a seven year option, exercisable at $33.065 per share. The other half was also a seven year option, exercisable at $33.065 but with an additional performance hurdle that the stock had to trade at an average of $50 and a little over $0.40 per share for 150 percent of the option exercise price for 90 consecutive days for the option to be exercisable.

Furthermore, these options, all of these options cliff vested at the end of five years, meaning that none of them could be exercised if Steve left the company. And at the time what it meant was that the stock had to trade in the high 40's for Steve to have a chance to realize that $10 million in value. And everybody's aware that the stock is way off and say at $11 or so, or a third of the option stock – the option strike price, the Office Depot stock price would have to approximately triple to get to the exercise strike price.

And in line with that, I'd like to also say that all of Steve Odland's options, all of them, since he joined the company, are significantly underwater and can have value only if the stock appreciates in a major way. And this is substantially the case for all executives and it shows that the company does support and does execute on the application of a pay for performance philosophy.

And Neil Austrian did comment on the backgrounds of some of the directors of Office Depot. I'd like to say, or add to that, or compliment his comments, just to say that the compensation committee is comprised of independent experienced and very highly motivated individuals who take their responsibilities very seriously. And you can see their backgrounds in the proxy.

But when you have a CEO, former CEO of Walgreen's and a chairman and CEO of Frito-Lay, a retired admiral from the Navy, who basically ran Human Relations for the Navy and was President of the Red Cross, and is a director of many public company's such as May Company, Lehman Brothers, Weight Watchers and others.

And Scott Hedrick, who was a founder and partner of InterWest, who served and chaired many compensation committees, I think you have to conclude that these are people with vast experience. They all have strong minds of their own and they're all totally committed to do the right thing and to follow through on the execution of pay for performance approach.

And so this has been, there's been confusion here because the actual pay has not been aligned correctly with the appropriate year. But if you do that you'll see that the pay for performance is in practice, executed totally.

CHEN: OK, we only have a few minutes left. I want to have this question asked that just came in through e-mail here. Have you engaged with a dissident to avoid contest?

AUSTRIAN: Can you repeat – have we engaged with a dissident to what?

CHEN: Yes. To avoid this proxy contest.

AUSTRIAN: This is Neil Austrian; Allen Levin called me after he started the proxy fight. I suggested to him that it might have been more appropriate to have called me earlier since I'm fairly available and fairly open.

And he suggested we meet, which I did and we met for lunch. And I asked Allen at that time, and I had another former board member with me, as to what his ultimate game plan was. And he responded that they really wanted to remove the CEO, which I didn't think made any sense at this point in time whatsoever.

After that lunch, we had one more conversation where he was somewhat disappointed, I guess, and all the fight letters that we had that just letters he was sending out from his side and we just agreed to disagree at that point and see what happened in terms of how our shareholders felt about our board and our management team.

UNIDENTIFIED PARTICIPANT: State that you're open.

I'm very open to discussing it and as I said, and I've said to many of our shareholders, this board is an open board. We welcome suggestions for people to add to our board. At this point in time, our board does not feel that either of these two gentlemen at this point in time adds anything to the board that's not currently on the board. And frankly if their intent is to unseat the CEO, it's a total disruption at this point in terms of achieving the operating results we all anticipate.

CHEN: OK. So we're actually running out of time. And we're through all the questions that we received. So if one of you would like to take a few minutes just to sum up your position I'd like to certainly offer that to you. And just in the time remaining if there are any other questions remaining you can e-mail them to us at proxytalk@glasslewis.com.

ODLAND: Yes, Warren, I would say that nobody in management is happy with the stock price the way it is. Nobody in management is happy with the performance in the back-half of 2007. We are very pleased with our record performance from 2004 to the beginning of 2007. We think that demonstrates our long term plan was working very well. We made progress on every metric that was laid out for us and is monitored by the board.

We built a strong management team. Everybody in the retail business has a career in retail. Everybody in the 'B' to 'B' business had a career in 'B' to 'B'. We recruited strong managing directors in every region internationally. And we have acknowledged the situation that has changed for us. We delivered all new plans in detailed to our shareholders.

We haven't posted all the details for everybody in the world to see, but our shareholders know the plans in detail.. We are executing those plans. We're seeing progress as we go forward and we are committed to turning this business around again for our share price to recover and we are committed to driving long term shareholder value for years to come.

Neil?

AUSTRIAN: I would just say from the board's standpoint, we can assure all of our stockholders; it's a very active, very engaged, highly motivated board. We're not happy with the stock price. We're not happy with where we are. We are happy that we've made some significant progress though in terms of the hand that we turned over to Steve at the time he was recruited.

If I come back, we now have a divisionally aligned group where Chuck Rubin's responsible for retail profits, Steve Schmidt for 'B' to 'B' profits; Charlie Brown for our international profits. We've integrated our acquisitions. We've eliminated duplicate overhead.

We have made significant progress on our IT systems and I have to remind you we had three or four different systems at the time the Guilbert acquisitions. It takes time to do it, its about a four or five year plan, which was laid out after you go back with your consultants and figure out exactly what you want to do.

For 2005, 2006 we significantly narrowed the gap on our operating margins vis-à-vis Staples and some of our other competitors. The shopping experience that Chuck Rubin talked about has increased dramatically from a consumer standpoint.

Steve's done a lot of good things. We are not happy with the second half of 2007. The board and management are committing to improving shareholder value.

CHEN: Well, thank you. Thank you very much. I want to thank all of our participants, Steve Odland and other representatives of Office Depot, which I won't name every single one. I appreciate the time you all took to participate and thanks to all of you who have participated in the call.

Just I want to make a quick note that we're hosting Proxy Talk regularly. Our next Proxy Talk will be this Thursday at 2:00 p.m. Eastern, with AFLAC, Incorporated, the chairman and CEO Daniel Amos to discuss the company's submission to shareholders of an advisory vote on company's compensation. So, for more information please e-mail proxytalk@glasslewis.com.

Thank you very much and this concludes today's call.

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