AVIS BUDGET GROUP, INC.
Form 10-Q
November 05, 2010
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

Form 10-Q

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

For the quarterly period ended September 30, 2010

OR

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

For the transition period from to

Commission File No. 1-10308

Avis Budget Group, Inc.

(Exact name of registrant as specified in its charter)

Delaware	**06-0918165**
(State or other jurisdiction of incorporation or organization)	*(I.R.S. Employer Identification Number)*

6 Sylvan Way

Parsippany, NJ	**07054**
(Address of principal executive offices)	*(Zip Code)*

(973) 496-4700

(Registrant s telephone number, including area code)

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 x 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 x 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	x	Accelerated filer	¨
Non-accelerated filer	¨	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 x

The number of shares outstanding of the issuer s common stock was 102,860,655 shares as of October 29, 2010.

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FORWARD-LOOKING STATEMENTS

The forward-looking statements contained herein are subject to known and unknown risks, uncertainties and other factors which may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. These forward-looking statements are based on various facts and were derived utilizing numerous important assumptions and other important factors that could cause actual results to differ materially from those in the forward-looking statements. Forward-looking statements include the information concerning our future financial performance, business strategy, projected plans and objectives. Statements preceded by, followed by or that otherwise include the words believes , expects , anticipates , intends , projects , estimates , plans , may increase and similar expressions or future or conditional verbs such as will , should , would , may and could are forward-looking in nature and not historical facts. You should understand that the following important factors and assumptions could affect our future results and could cause actual results to differ materially from those expressed in such forward-looking statements:

- the high level of competition in the vehicle rental industry and the impact such competition may have on pricing and rental volume;
- an increase in our fleet costs as a result of an increase in the cost of new vehicles and/or a decrease in the price at which we dispose of used vehicles either in the used vehicle market or under repurchase or guaranteed depreciation programs;
- the results of operations or financial condition of the manufacturers of our cars, which could impact their ability to perform their payment obligations under repurchase and/or guaranteed depreciation arrangements they have with us, and/or their willingness or ability to make cars available to us or the rental car industry as a whole on commercially reasonable terms or at all;
- travel demand, including airline passenger traffic in the United States and in the other international locations in which we operate;
- the effects of economic conditions, including in the housing market, and the impact such conditions may have on us, particularly during our peak season or in key market segments;
- our ability to obtain financing for our operations, including the funding of our vehicle fleet via the asset-backed securities and lending market consistent with current costs, and the financial condition of financial-guaranty firms that have insured a portion of our outstanding vehicle-backed debt;
- an occurrence or threat of terrorism, pandemic disease, natural disasters or military conflict in the locations in which we operate;
- our dependence on third-party distribution channels;
- our ability to control costs through our cost-savings and efficiency improvement initiatives or otherwise and successfully implement our business strategy;
- our ability to utilize derivative instruments and the impact of derivative instruments we currently utilize, which can be affected by fluctuations in interest rates, changes in government regulations and other factors;

our ability to accurately estimate our future results;

a major disruption in our communication or centralized information networks;

our exposure to uninsured claims in excess of historical levels;

our failure or inability to comply with regulations or contractual obligations or any changes in regulations or contractual obligations, including with respect to personally identifiable information;

any impact on us from the actions of our licensees, dealers and independent contractors;

substantial increases in the cost, or decreases in the supply, of fuel, vehicle parts, energy or other resources on which we depend to operate our business;

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- risks related to our indebtedness, including our substantial amount of debt and our ability to incur substantially more debt;

- our ability to meet the financial and other covenants contained in the agreements governing our indebtedness;

- the terms of agreements among us and our former real estate, hospitality and travel distribution businesses following the separation of those businesses from us during third quarter 2006, when we were known as Cendant Corporation, particularly with respect to the allocation of assets and liabilities, including contingent liabilities and guarantees, commercial arrangements, the ability of each of the separated companies to perform its obligations, including its indemnification obligations, under these agreements, and the former real estate business right to control the process for resolving disputes related to contingent liabilities and assets;

- risks associated with litigation involving the Company;

- risks related to tax obligations and the effect of potential changes in accounting standards;

- risks related to the proposed acquisition of Dollar Thrifty Automotive Group, Inc. (Dollar Thrifty), including the timing to consummate such acquisition, the ability and timing to obtain required regulatory approvals and financing (and any conditions thereto), and our ability to promptly and effectively integrate the businesses of Dollar Thrifty and Avis Budget Group;

- our exposure to fluctuations in foreign exchange rates; and

- other business, economic, competitive, governmental, regulatory, political or technological factors affecting our operations, pricing or services.

Other factors and assumptions not identified above, including those described under Risk Factors and Management s Discussion and Analysis of Financial Condition and Results of Operations in our 2009 Annual Report on Form 10-K and this Quarterly Report on Form 10-Q were also involved in the derivation of these forward-looking statements, and the failure of such other assumptions to be realized, as well as other factors, may also cause actual results to differ materially from those projected. Most of these factors are difficult to predict accurately and are generally beyond our control.

You should consider the areas of risk described above, as well as those described under Risk Factors and Management s Discussion and Analysis of Financial Condition and Results of Operations in our 2009 Annual Report on Form 10-K and this Quarterly Report on Form 10-Q and those that may be disclosed from time to time in filings with the Securities and Exchange Commission, in connection with any forward-looking statements that may be made by us and our businesses generally. Except to the extent of our obligations under the federal securities laws, we undertake no obligation to release any revisions to any forward-looking statements, to report events or to report the occurrence of unanticipated events. For any forward-looking statements contained in any document, we claim the protection of the safe harbor for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995.

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PART I FINANCIAL INFORMATION

Item 1. Financial Statements

Avis Budget Group, Inc.

CONSOLIDATED CONDENSED STATEMENTS OF INCOME

(In millions, except per share data)

(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	**2009**	**2010**	**2009**
Revenues				
Vehicle rental	$ 1,145	$ 1,123	$ 2,972	$ 3,036
Other	367	342	987	935
Net revenues	1,512	1,465	3,959	3,971
Expenses				
Operating	705	731	1,956	2,020
Vehicle depreciation and lease charges, net	352	357	988	1,104
Selling, general and administrative	161	155	438	421
Vehicle interest, net	80	75	230	215
Non-vehicle related depreciation and amortization	24	26	70	71
Interest expense related to corporate debt, net				
Interest expense	40	37	122	114
Early extinguishment of debt			40	
Restructuring charges	6	1	9	14
Impairment				1
Total expenses	1,368	1,382	3,853	3,960
Income before income taxes	144	83	106	11
Provision for income taxes	54	26	28	9
Net income	$ 90	$ 57	$ 78	$ 2
Earnings per share				
Basic	$ 0.88	$ 0.55	$ 0.76	$ 0.02
Diluted	$ 0.73	$ 0.54	$ 0.66	$ 0.02

See Notes to Consolidated Condensed Financial Statements (Unaudited).

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Avis Budget Group, Inc.

CONSOLIDATED CONDENSED BALANCE SHEETS

(In millions, except share data)

(Unaudited)

	September 30, 2010	December 31, 2009
Assets		
Current assets:		
Cash and cash equivalents	$ 623	$ 482
Receivables, net	317	290
Deferred income taxes	107	107
Other current assets	300	851
Total current assets	1,347	1,730
Property and equipment, net	418	442
Deferred income taxes	544	597
Goodwill	76	76
Other intangibles, net	479	478
Other non-current assets	244	248
Total assets exclusive of assets under vehicle programs	3,108	3,571
Assets under vehicle programs:		
Program cash	43	157
Vehicles, net	7,069	5,967
Receivables from vehicle manufacturers and other	211	170
Investment in Avis Budget Rental Car Funding (AESOP) LLC related party	270	228
	7,593	6,522
Total assets	$ 10,701	$ 10,093
Liabilities and stockholders equity		
Current liabilities:		
Accounts payable and other current liabilities	$ 928	$ 1,272
Current portion of long-term debt	9	12
Total current liabilities	937	1,284
Long-term debt	2,119	2,119
Other non-current liabilities	548	630
Total liabilities exclusive of liabilities under vehicle programs	3,604	4,033
Liabilities under vehicle programs:		

Debt	706	714
Debt due to Avis Budget Rental Car Funding (AESOP) LLC related party	4,571	3,660
Deferred income taxes	1,287	1,267
Other	160	197
	6,724	5,838
Commitments and contingencies (Note 13)		
Stockholders equity		
Preferred stock, $.01 par value authorized 10 million shares; none issued and outstanding		
Common stock, $.01 par value authorized 250 million shares; issued 136,970,259 and 136,931,540 shares	1	1
Additional paid-in capital	8,906	9,098
Accumulated deficit	(2,613)	(2,691)
Accumulated other comprehensive income (loss)	42	(37)
Treasury stock, at cost 33,744,683 and 34,612,016 shares	(5,963)	(6,149)
Total stockholders equity	373	222
Total liabilities and stockholders equity	$ 10,701	$ 10,093

See Notes to Consolidated Condensed Financial Statements (Unaudited).

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Avis Budget Group, Inc.

CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS

(In millions)

(Unaudited)

	Nine Months Ended September 30, 2010	Nine Months Ended September 30, 2009
Operating Activities		
Net income	$ 78	$ 2
Adjustments to reconcile net income to net cash provided by operating activities exclusive of vehicle programs:		
Non-vehicle related depreciation and amortization	70	71
Net change in assets and liabilities, excluding the impact of acquisitions and dispositions:		
Receivables	(34)	25
Income taxes and deferred income taxes	(93)	(8)
Accounts payable and other current liabilities	107	30
Reimbursement from Realogy and Wyndham for taxes paid	99	
Reimbursement from Wyndham for tax attributes	86	
Other, net	44	34
Net cash provided by operating activities exclusive of vehicle programs	357	154
Vehicle programs:		
Vehicle depreciation	981	1,096
	981	1,096
Net cash provided by operating activities	1,338	1,250
Investing Activities		
Property and equipment additions	(39)	(19)
Net assets acquired, net of cash acquired and acquisition related payments	(2)	
Proceeds received on asset sales	11	10
Other, net	(5)	
Net cash used in investing activities exclusive of vehicle programs	(35)	(9)
Vehicle programs:		
Decrease in program cash	123	5
Investment in vehicles	(6,549)	(5,019)
Proceeds received on disposition of vehicles	4,445	5,424
Investment in debt securities of Avis Budget Rental Car Funding (AESOP) related party	(380)	
Proceeds from debt securities of Avis Budget Rental Car Funding (AESOP) related party	380	
Distribution from Avis Budget Rental Car Funding (AESOP) LLC related party		19

	(1,981)	429
Net cash provided by (used in) investing activities	(2,016)	420

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Avis Budget Group, Inc.

CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS (Continued)

(In millions)

(Unaudited)

	Nine Months Ended September 30, 2010	Nine Months Ended September 30, 2009
Financing Activities		
Proceeds from borrowings	444	100
Principal payments on borrowings	(458)	(8)
Debt financing fees	(32)	
Other, net	4	(2)
Net cash provided by (used in) financing activities exclusive of vehicle programs	(42)	90
Vehicle programs:		
Proceeds from borrowings	7,196	5,728
Principal payments on borrowings	(6,391)	(7,335)
Net change in short-term borrowings	67	36
Other, net	(17)	(6)
	855	(1,577)
Net cash provided by (used in) financing activities	813	(1,487)
Effect of changes in exchange rates on cash and cash equivalents	6	29
Net increase in cash and cash equivalents	141	212
Cash and cash equivalents, beginning of period	482	258
Cash and cash equivalents, end of period	$ 623	$ 470

See Notes to Consolidated Condensed Financial Statements (Unaudited).

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Avis Budget Group, Inc.

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Unaudited)

(Unless otherwise noted, all dollar amounts in tables are in millions, except per share amounts)

1. Basis of Presentation and Recently Issued Accounting Pronouncements

Basis of Presentation

Avis Budget Group, Inc. provides car and truck rentals and ancillary services to businesses and consumers in the United States and internationally. The accompanying unaudited Consolidated Condensed Financial Statements include the accounts and transactions of Avis Budget Group, Inc. and its subsidiaries (Avis Budget), as well as entities in which Avis Budget directly or indirectly has a controlling financial interest (collectively, the Company), and have been prepared pursuant to the rules and regulations of the U.S. Securities and Exchange Commission (SEC) for interim financial reporting.

The Company operates in the following business segments:

Domestic Car Rental provides car rentals and ancillary products and services in the United States.

International Car Rental provides vehicle rentals and ancillary products and services primarily in Argentina, Australia, Canada, New Zealand, Puerto Rico and the U.S. Virgin Islands.

Truck Rental provides truck rentals and related services to consumers and light commercial users in the United States.

In presenting the Consolidated Condensed Financial Statements in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP), management makes estimates and assumptions that affect the amounts reported and related disclosures. Estimates, by their nature, are based on judgments and available information. Accordingly, actual results could differ from those estimates. In management s opinion, the Consolidated Condensed Financial Statements contain all normal recurring adjustments necessary for a fair presentation of interim results reported. The results of operations reported for interim periods are not necessarily indicative of the results of operations for the entire year or any subsequent interim period. These financial statements should be read in conjunction with the Company s 2009 Annual Report on Form 10-K filed on February 24, 2010.

Vehicle Programs. The Company presents separately the financial data of its vehicle programs. These programs are distinct from the Company s other activities since the assets under vehicle programs are generally funded through the issuance of debt that is collateralized by such assets. The income generated by these assets is used, in part, to repay the principal and interest associated with the debt. Cash inflows and outflows relating to the generation or acquisition of such assets and the principal debt repayment or financing of such assets are classified as activities of the Company s vehicle programs. The Company believes it is appropriate to segregate the financial data of its vehicle programs because, ultimately, the source of repayment of such debt is the realization of such assets.

Separation. In connection with the separation of Cendant Corporation (as the Company was formerly known) into four independent companies (the Separation), the Company completed the spin-offs of Realogy Corporation (Realogy) and Wyndham Worldwide Corporation (Wyndham) on July 31, 2006 and completed the sale of Travelport, Inc. (Travelport) on August 23, 2006.

Adoption of New Accounting Standards during 2010

In June 2009, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2009-16, Accounting for Transfers of Financial Assets . The Company adopted this guidance on January 1, 2010, as required, and it did not have a significant impact on its financial statements.

In December 2009, the FASB issued ASU No. 2009-17, Accounting by Enterprises Involved with Variable Interest Entities . The Company adopted this guidance on January 1, 2010, as required, and it did not have a significant impact on its financial statements.

In February 2010, the FASB issued ASU No. 2010-09, Subsequent Events Amendments to Certain Recognition and Disclosure Requirements . The Company adopted this guidance upon its issuance, as required, and it did not have a significant impact on its financial statements.

In January 2010, the FASB issued ASU No. 2010-06, Fair Value Measurements and Disclosures , which will expand fair value disclosures, requiring companies to provide (i) information about movements of assets between levels 1 and 2, (ii) a reconciliation of purchases, sales, issuance and settlements for all level 3 instruments and (iii) fair value measurement disclosures for each class of assets and liabilities. The Company adopted this guidance on January 1, 2010, as required, except for the disclosures about purchases, sales, issuances and settlements for level 3 instruments and fair value measurements, which will be adopted on January 1, 2011, as required, and it did not have, and is not expected to have, a significant impact on its financial statements.

2. Restructuring Charges

Beginning in late 2008, the Company implemented initiatives within the Company s Domestic Car Rental, International Car Rental and Truck Rental segments to reduce costs, enhance organizational efficiency and consolidate and rationalize existing processes and facilities. During the nine months ended September 30, 2010, as part of this process, the Company formally communicated the termination of employment to approximately 1,200 employees within its Domestic Car Rental segment and incurred $9 million in restructuring charges, the majority of which is expected to be cash. These charges primarily represent costs associated with the closure and consolidation of certain back-office administrative facilities and severance, outplacement services and other costs associated with the employee terminations. As of September 30, 2010, the Company had terminated approximately 1,100 of these employees.

At September 30, 2010, the remaining liability relating to restructuring actions amounted to $6 million, primarily for lease obligation costs related to vacated locations which are expected to be paid through 2018. As part of this process, the Company continues to implement steps to reduce costs and consolidate certain customer facing and non-customer facing activities and locations. The Company expects further restructuring costs related to this process of approximately $2 million to be incurred through December 31, 2010.

The restructuring charges and corresponding utilization are recorded within the Company s segments as follows:

	Domestic Car Rental	International Car Rental	Truck Rental	Total
Balance as of January 1, 2010	$ 3	$ 1	$ 1	$ 5
Incremental charges	9			9
Cash payment/utilization	(6)	(1)	(1)	(8)
Balance as of September 30, 2010	$ 6	$	$	$ 6

The restructuring charges and the corresponding utilization are summarized by category as follows:

	Personnel Related	Facility Related	Total
Balance as of January 1, 2010	$ 1	$ 4	$ 5
Incremental charges	4	5	9
Cash payment/utilization	(4)	(4)	(8)
Balance as of September 30, 2010	$ 1	$ 5	$ 6

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3. Earnings Per Share

The following table sets forth the computation of basic and diluted earnings per share (EPS):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Net income for basic EPS	$ 90	$ 57	$ 78	$ 2
Convertible debt interest, net of tax	2		6	
Net income for diluted EPS	$ 92	$ 57	$ 84	$ 2
Basic weighted average shares outstanding	103.2	102.3	103.0	102.1
Options, warrants and non-vested stock	2.2	2.2	2.2	1.3
Convertible debt	21.2		21.2	
Diluted weighted average shares outstanding	126.6	104.5	126.4	103.4
Earnings per share:				
Basic	$ 0.88	$ 0.55	$ 0.76	$ 0.02
Diluted	$ 0.73	$ 0.54	$ 0.66	$ 0.02

The following table summarizes the Company s outstanding common stock equivalents that were anti-dilutive and therefore excluded from the computation of diluted EPS:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Options [(a)]	2.0	3.4	2.0	3.4
Warrants [(b)]	21.2		21.2	

(a) The weighted average exercise price for anti-dilutive options for the three and nine months ended September 30, 2010 was $20.92. For the three and nine months ended September 30, 2009, the weighted average exercise price for anti-dilutive options was $24.48.

(b) Represents all outstanding warrants for the three and nine months ended September 30, 2010. The exercise price for the warrants outstanding for the three and nine months ended September 30, 2010 was $22.50.

4. Intangible Assets

Intangible assets consisted of:

	As of September 30, 2010			As of December 31, 2009		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Amortizable Intangible Assets						
Franchise agreements	$ 73	$ 24	$ 49	$ 73	$ 22	$ 51

Customer lists	19	9	10	19	9	10
Other	2	1	1	2	1	1
	$ 94	$ 34	$ 60	$ 94	$ 32	$ 62
Unamortizable Intangible Assets						
Goodwill	$ 76			$ 76		
Trademarks [a]	$ 419			$ 416		

(a) The increase in trademarks is primarily due to a $2 million increase from fluctuations in foreign currency rates and $1 million in acquisitions during 2010.

Amortization expense relating to all intangible assets was approximately $1 million during third quarter 2010 and 2009. For the nine months ended September 30, 2010 and 2009, amortization expense was approximately $2 million.

Based on the Company s amortizable intangible assets at September 30, 2010, the Company expects amortization expense of approximately $1 million for the remainder of 2010 and approximately $3 million for each of the five fiscal years thereafter.

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5. Financial Instruments

The fair value of the Company s financial instruments is generally determined by reference to market values resulting from trading on a national securities exchange or in an over-the-counter market. In some cases where quoted market prices are not available, prices are derived by considering the yield of the benchmark security that was initially used to price the instruments and adjusting this rate by the credit spread that market participants would demand for the instruments as of the measurement date. The carrying amounts of cash and cash equivalents, accounts receivable, program cash and accounts payable and accrued liabilities approximate fair value due to the short-term maturities of these assets and liabilities.

Debt Instruments

The carrying amounts and estimated fair values of debt instruments are as follows:

	As of September 30, 2010		As of December 31, 2009	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Corporate debt				
Current portion of long-term debt	$ 9	$ 9	$ 12	$ 12
Long-term debt, excluding convertible debt	1,774	1,786	1,774	1,675
Convertible debt	345	362	345	376
Debt under vehicle programs				
Vehicle-backed debt due to Avis Budget Rental Car Funding (AESOP) LLC	$ 4,571	$ 4,649	$ 3,660	$ 3,634
Vehicle-backed debt	704	715	705	707

Derivative instruments and hedging activities

The Company uses foreign exchange forward contracts to manage its exposure to changes in foreign currency exchange rates associated with its foreign currency denominated receivables and forecasted royalties, forecasted earnings of foreign subsidiaries and forecasted foreign currency denominated acquisitions. The Company primarily hedges its foreign currency exposure to the Canadian, Australian and New Zealand dollars. The majority of forward contracts do not qualify for hedge accounting treatment. The fluctuations in the value of these forward contracts do, however, largely offset the impact of changes in the value of the underlying risk they economically hedge. Forward contracts used to hedge forecasted third party receipts and disbursements up to twelve months are designated and do qualify as cash flow hedges. The amount of gains or losses reclassified from accumulated other comprehensive income to earnings resulting from ineffectiveness or from excluding a component of the forward contracts gain or loss from the effectiveness calculation for cash flow hedges during the three and nine months ended September 30, 2010 and 2009 was not material, nor is the amount of gains or losses the Company expects to reclassify from accumulated other comprehensive income to earnings over the next twelve months.

The Company uses various hedging strategies including interest rate swaps and interest rate caps to create an appropriate mix of fixed and floating rate assets and liabilities. The Company uses interest rate swaps, designated as cash flow hedges, to manage the risk related to its floating rate corporate debt. In connection with such cash flow hedges, the Company records changes in the intrinsic value of these cash flow hedges to other comprehensive income, net of tax, and subsequently reclassifies these amounts into earnings in the period during which the hedged transaction is recognized. The changes in fair values of hedges that were determined to be ineffective are immediately reclassified from accumulated other comprehensive income into earnings. In first quarter 2010, the Company reclassified $36 million from accumulated other comprehensive income to earnings in connection with the early termination of certain interest rate swaps related to the repayment of a portion of the Company s floating rate term loan. The Company estimates that approximately $71 million of losses deferred in accumulated other comprehensive income will be recognized over the next twelve months, which is expected to be offset in earnings by the impact of the underlying hedged items.

To manage the risk associated with its floating rate vehicle-backed debt, the Company uses derivatives. These derivatives include freestanding derivatives and derivatives designated as cash flow hedges. In connection with such cash flow hedges, the Company records the effective portion of the change in fair value in other comprehensive income, net of tax. The Company records the change in fair value gains or losses related to freestanding derivatives in its consolidated results of operations.

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The Company periodically enters into derivative commodity contracts to manage its exposure to changes in the price of unleaded gasoline. These instruments were designated as freestanding derivatives and the changes in fair value are recorded in the Company s consolidated results of operations.

Certain of the Company s derivative instruments contain collateral support provisions that require the Company to post cash collateral to the extent that these derivatives are in a liability position. The aggregate fair value of such derivatives that are in a liability position and the aggregate fair value of assets needed to settle these derivatives as of September 30, 2010 was approximately $8 million, for which the Company has posted cash collateral in the same amount in the normal course of business.

As of September 30, 2010, the Company held derivative instruments with notional values as follows: interest rate caps of approximately $2.7 billion, interest rate swaps of $587 million, foreign exchange swaps of $75 million, foreign exchange forward contracts of $10 million and commodity contracts for the purchase of 3 million gallons of unleaded gasoline.

The Company used significant observable inputs (level 2 inputs) to determine the fair value of its derivative assets and liabilities. Derivatives entered into by the Company are typically executed over-the-counter and are valued using internal valuation techniques, as no quoted market prices exist for such instruments. The valuation technique and inputs depend on the type of derivative and the nature of the underlying exposure. The principal techniques used to value these instruments are discounted cash flows and Black-Scholes option valuation models. These models take into account a variety of factors including, where applicable, maturity, commodity prices, interest rate yield curves, credit curves of the Company and counterparties, counterparty creditworthiness and forward and spot currency exchange rates. These factors are applied on a consistent basis and are based upon observable inputs where available.

Fair values of derivative instruments are as follows:

	As of September 30, 2010		As of December 31, 2009	
	Fair Value, Asset Derivatives	**Fair Value, Liability Derivatives**	**Fair Value, Asset Derivatives**	**Fair Value, Liability Derivatives**
Derivatives designated as hedging instruments [a]				
Interest rate swaps [b]	$	$ 9	$	$ 39
Derivatives not designated as hedging instruments [a]				
Interest rate swaps [c]		1		
Interest rate contracts [c]	1	1		9
Total	$ 1	$ 11	$	$ 48

(a) Amounts in this table exclude derivatives issued by Avis Budget Rental Car Funding (AESOP) LLC (Avis Budget Rental Car Funding), as it is not consolidated by the Company; however, certain amounts related to the derivatives held by Avis Budget Rental Car Funding are included within accumulated other comprehensive income, as discussed in Note 14 Stockholders Equity.

(b) Included in other non-current liabilities.

(c) Included in assets under vehicle programs and liabilities under vehicle programs.

The effect of derivative instruments not designated as hedging instruments in the Company s consolidated results of operations for the three months ended September 30, 2010 was (i) a $15 million gain recognized as a component of operating expenses related to foreign exchange swaps and foreign exchange forward contracts, (ii) an immaterial gain recognized as a component of operating expenses related to our commodity contracts, and (iii) an immaterial loss recognized as a component of interest expense related to interest rate swaps and interest rate caps not designated as hedging instruments. The gain on foreign exchange swaps and foreign exchange forward contracts was largely offset by foreign currency exchange losses on the underlying hedged items, primarily intracompany loans.

The effect of derivative instruments not designated as hedging instruments in the Company s consolidated results of operations for the nine months ended September 30, 2010 was (i) a $14 million gain recognized as a component of operating expenses related to foreign exchange swaps and foreign exchange forward contracts, (ii) an immaterial gain recognized as a component of operating expenses related to our commodity contracts and (iii) a loss of $2 million recognized as a component of interest expense related to interest rate swaps and interest rate caps not designated as hedging instruments. The gain on foreign exchange swaps and foreign exchange forward contracts was largely offset by foreign currency exchange losses on the underlying hedged items, primarily intracompany loans.

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The Company also recognized unrealized gains of $8 million and $22 million, as a component of other comprehensive income, net of tax, during the three and nine months ended September 30, 2010, respectively, which relate to interest rate swaps designated as cash flow hedges.

The effect of derivative instruments in the Company s consolidated results of operations for the three months ended September 30, 2009, was (i) a loss of $1 million recognized as a component of operating expenses related to foreign exchange forward contracts, (ii) an insignificant loss recognized as a component of operating expenses related to our commodity contracts and (iii) a $2 million loss recognized as a component of interest expense related to interest rate swaps not designated as hedging instruments.

The effect of derivative instruments in the Company s consolidated results of operations for the nine months ended September 30, 2009, was (i) a loss of $5 million recognized as a component of operating expenses related to foreign exchange forward contracts, (ii) a gain of $3 million recognized as a component of operating expenses related to our commodity contracts and (iii) a loss of $4 million recognized as a component of interest expense related to interest rate swaps not designated as hedging instruments.

The Company also recognized unrealized gains of $2 million and $26 million, as a component of other comprehensive income, net of tax, for the three and nine months ended September 30, 2009, respectively, which relate to interest rate swaps designated as cash flow hedges.

6. Vehicle Rental Activities

The components of the Company s vehicles, net within assets under vehicle programs are as follows:

	As of September 30, 2010	As of December 31, 2009
Rental vehicles	$ 7,809	$ 6,090
Less: Accumulated depreciation	(1,131)	(945)
	6,678	5,145
Vehicles held for sale	391	822
Vehicles, net	$ 7,069	$ 5,967

The components of vehicle depreciation and lease charges, net are summarized below:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Depreciation expense	$ 355	$ 363	$ 981	$ 1,096
Lease charges	6	23	25	37
Gain on sales of vehicles, net and vehicle disposition costs	(9)	(29)	(18)	(29)
Vehicle depreciation and lease charges, net	$ 352	$ 357	$ 988	$ 1,104

For the three months ended September 30, 2010 and 2009, vehicle interest, net on the accompanying Consolidated Condensed Statements of Income excludes $43 million and $38 million, respectively, and for the nine months ended September 30, 2010 and 2009, excludes $127 million and $116 million respectively, of interest expense related to the Company s convertible senior notes and the fixed and floating rate borrowings of the Company s Avis Budget Car Rental, LLC (Avis Budget Car Rental) subsidiary. Such interest is recorded within interest expense related to corporate debt, net.

7. Income Taxes

During third quarter 2010, the Company reached a settlement with the Internal Revenue Service (IRS) with respect to its examination of the Company s taxable years 2003 through 2006, the year of the Separation. The Company was entitled to indemnification for most pre-Separation tax matters from Realogy and Wyndham and therefore the conclusion of the audit did not have a material impact to the Company s financial position. The Company made payments to the IRS of $116 million, including interest, in conjunction with the conclusion of the audit, all of which were funded by Realogy and Wyndham. The Company was also reimbursed $86 million by Wyndham for the use of certain of the Company s tax attributes in connection with the conclusion of the IRS audit. As a result of the conclusion of the audit, the Company reduced income taxes payable and related receivables from Realogy and Wyndham by approximately $295 million, which items offset within income from discontinued operations. In addition, in connection with the conclusion of the IRS audit, a reallocation of certain deferred tax balances with our former subsidiaries resulted in a $16 million decrease to stockholders equity. The reductions in income taxes payable and receivables from Realogy and Wyndham are reflected in accounts payable and other current liabilities, and other current assets, respectively, as of September 30, 2010.

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The following is a reconciliation of the total amounts of unrecognized tax benefits:

Balance at January 1, 2010	$ 603
Additions based on tax positions related to the current year	
Additions for tax positions for prior years	7
Reductions for tax positions for prior years	(434)
Settlements	(100)
Balance at September 30, 2010	$ 76

The Company s effective tax rate for the nine months ended September 30, 2010 is a provision of 26.4%. Such rate differs from the Federal statutory rate of 35.0% primarily due to an $11 million benefit relating to additional tax depreciation within the Company s operations in Australia.

The Company s effective tax rate from continuing operations for the nine months ended September 30, 2009 is a provision of 81.8%. Such rate differs from the Federal statutory rate of 35.0% primarily due to foreign withholding taxes and the differences in the amount of stock-based compensation recorded for book and tax purposes.

8. Other Current Assets

Other current assets consisted of:

	As of September 30, 2010	As of December 31, 2009
Prepaid expenses	$ 145	$ 127
Receivables from Wyndham [(a)]	45	249
Receivables from Realogy [(a)]	34	410
Other	76	65
	$ 300	$ 851

(a) Represents amounts due for certain contingent and other corporate liabilities assumed by Realogy and Wyndham in connection with the Separation. These amounts are due from Realogy and Wyndham on demand upon the Company s settlement of the related liability. At September 30, 2010 and December 31, 2009, there are corresponding liabilities recorded within accounts payable and other current liabilities. Realogy has posted a letter of credit for the benefit of the Company to cover Realogy s performance in respect of these receivables, as more fully described under Note 13 Commitments and Contingencies. During third quarter 2010, in connection with the conclusion of the IRS audit, the Company reduced its income taxes payable and the related receivables from Realogy and Wyndham.

9. Accounts Payable and Other Current Liabilities

Accounts payable and other current liabilities consisted of:

	As of September 30, 2010	As of December 31, 2009
Accounts payable	$ 190	$ 151
Accrued payroll and related	155	145
Public liability and property damage insurance liabilities current	97	97
Income taxes payable current[a]	29	399
Accrued interest related to tax contingencies [a]	8	89
Other	449	391
	$ 928	$ 1,272

[a] During third quarter 2010, the Company decreased income taxes payable and accrued interest related to tax contingencies by $358 million and $81 million, respectively, and decreased the related receivables from Realogy and Wyndham, due to the conclusion of the IRS audit.

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10. Other Non-Current Liabilities
Other non-current liabilities consisted of:

	As of September 30, 2010	As of December 31, 2009
Public liability and property damage insurance liabilities	$ 210	$ 211
Pension liability	60	58
Acquisition related liabilities	55	57
Income taxes payable	45	100
Accrued interest related to tax contingencies	43	41
Other	135	163
	$ 548	$ 630

11. Long-term Debt and Borrowing Arrangements
Long-term debt consisted of:

	Maturity	As of September 30, 2010	As of December 31, 2009
Floating rate term loan [(a)]	April 2012	$ 52	$ 778
Floating rate term loan [(a)]	April 2014	271	
Floating rate notes	May 2014	250	250
7 5/8 % notes	May 2014	375	375
3 1/2% convertible notes	October 2014	345	345
7 3/4% notes	May 2016	375	375
9 5/8 % notes	March 2018	444	
		2,112	2,123
Other		16	8
Total long-term debt		2,128	2,131
Less: Current portion		9	12
Long-term debt		$ 2,119	$ 2,119

(a) The floating rate term loans and our revolving credit facilities are secured by pledges of all of the capital stock of all of the Company s direct or indirect domestic subsidiaries and up to 66% of the capital stock of each foreign subsidiary directly owned by the Company s domestic subsidiaries, subject to certain exceptions, and liens on substantially all of the Company s intellectual property and certain other real and personal property. In March 2010, the Company repaid $451 million of outstanding indebtedness under its floating rate term loan and the term loan outstanding subsequent to such repayment was amended with $52 million maturing in April 2012 and the balance maturing in April 2014. The floating rate term loan due 2012 bears interest at three month LIBOR plus 375 basis points, for a rate of 4.04% at September 30, 2010, and the floating rate term loan due 2014 bears interest at the greater of three month LIBOR or 1.50%, plus 425 basis points, for a rate of 5.75% at September 30, 2010.

During March 2010, the Company issued $450 million aggregate principal amount of 9 $^{5}/8$% Senior Notes due 2018. The notes pay interest semi-annually on March 15 and September 15 of each year, beginning September 2010. The notes are unsecured obligations of Avis Budget Car Rental and are guaranteed on a senior basis by the Company and certain of its domestic subsidiaries. These notes were issued at approximately 98.6% of par and the proceeds were used primarily to repay a portion of the Company s floating rate term loan. The notes rank equally with all existing and future senior unsecured indebtedness and are senior to all existing and future subordinated indebtedness. The Company has the right to redeem these notes in whole or in part at any time at the applicable redemption price plus any accrued and unpaid interest through the redemption date. In connection with the sale of the notes, the Company entered into a Registration Rights Agreement, pursuant to which it exchanged the originally issued notes for new notes which have been registered under the Securities Act of 1933, as amended, in August 2010. The terms of the new notes are substantially identical to those of the originally issued notes except that the transfer restrictions and registration rights provisions relating to the originally issued notes do not apply to the new notes.

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Committed Credit Facilities and Available Funding Arrangements

At September 30, 2010, the committed credit facilities available to the Company and/or its subsidiaries at the corporate or Avis Budget Car Rental level were as follows:

	Total Capacity	Outstanding Borrowings	Letters of Credit Issued	Available Capacity
Revolving credit facility maturing 2011 [(a) (c)]	$ 192	$	$ 73	$ 119
Revolving credit facility maturing 2013 [(b) (c)]	983		374	609

(a) This revolving credit facility expires in April 2011 and bears interest of one month LIBOR plus 400 basis points.

(b) This revolving credit facility, which is the portion of the pre-existing revolving credit facility that was amended in March 2010 to extend its maturity by two years (to April 2013), bears interest of one month LIBOR plus 450 basis points.

(c) The senior credit facilities, which encompass the floating rate term loans and the revolving credit facilities, are secured by pledges of all of the capital stock of all of the Company s direct or indirect domestic subsidiaries and up to 66% of the capital stock of each foreign subsidiary directly owned by the Company s domestic subsidiaries, subject to certain exceptions, and liens on substantially all of the Company s intellectual property and certain other real and personal property.

The Company s debt agreements contain restrictive covenants, including restrictions on dividends paid to the Company by certain of its subsidiaries, the incurrence of additional indebtedness by the Company and certain of its subsidiaries, acquisitions, mergers, liquidations, and sale and leaseback transactions. The Company s senior credit facilities contain maximum leverage and minimum coverage ratio requirements. The indentures governing the Company s senior unsecured notes, among other things, limit its ability to incur additional debt, subject to certain exceptions. As of September 30, 2010, the Company was in compliance with the financial covenants of its senior credit facilities.

12. Debt Under Vehicle Programs and Borrowing Arrangements

Debt under vehicle programs (including related party debt due to Avis Budget Rental Car Funding) consisted of:

	As of September 30, 2010	As of December 31, 2009
Debt due to Avis Budget Rental Car Funding [(a)]	$ 4,571	$ 3,660
Budget Truck financing:		
Budget Truck Funding program	223	220