NCR CORP
Form 10-Q
October 30, 2009

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, 2009

Commission File Number 001-00395

NCR CORPORATION

(Exact name of registrant as specified in its charter)

Maryland	**31-0387920**
(State or other jurisdiction of	**(I.R.S. Employer**

incorporation or organization)	**Identification No.)**

1700 South Patterson Blvd.

Dayton, Ohio 45479

(Address of principal executive offices) (Zip Code)

Registrant s telephone number, including area code: (937) 445-5000

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 to its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or such shorter period that the registrant was required to submit and post such files) Yes ¨ No ¨

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

Large accelerated filer	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

Number of shares of common stock, $0.01 par value per share, outstanding as of October 13, 2009, was approximately 159.2 million.

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Part I. Financial Information

Item 1. Financial Statements

Condensed Consolidated Statements of Operations (Unaudited)

In millions, except per share amounts

	Three Months Ended September 30		Nine Months Ended September 30	
	2009	2008	2009	2008
Product revenue	$ 541	$ 757	$ 1,539	$ 2,064
Service revenue	594	622	1,728	1,830
Total revenue	1,135	1,379	3,267	3,894
Cost of products	433	560	1,226	1,513
Cost of services	478	509	1,404	1,525
Selling, general and administrative expenses	159	175	474	518
Research and development expenses	36	35	105	111
Total operating expenses	1,106	1,279	3,209	3,667
Income from operations	29	100	58	227
Interest expense	-	6	10	17
Other expense (income), net	24	(5)	20	(16)
Income from continuing operations before income taxes	5	99	28	226
Income tax (benefit) expense	(12)	17	1	51
Income from continuing operations	17	82	27	175
Loss from discontinued operations, net of tax	-	(2)	-	(4)
Net income	17	80	27	171
Net income (loss) attributable to noncontrolling interests	2	-	4	(1)
Net income attributable to NCR	$ 15	$ 80	$ 23	$ 172
Amounts attributable to NCR common stockholders:				
Income from continuing operations	$ 15	$ 82	$ 23	$ 176
Loss from discontinued operations, net of tax	-	(2)	-	(4)
Net income	$ 15	$ 80	$ 23	$ 172
Income per share attributable to NCR common stockholders:				
Income per common share from continuing operations				
Basic	$ 0.09	$ 0.50	$ 0.14	$ 1.05
Diluted	$ 0.09	$ 0.49	$ 0.14	$ 1.03

Net income per common share				
Basic	$ 0.09	$ 0.49	$ 0.14	$ 1.03
Diluted	$ 0.09	$ 0.48	$ 0.14	$ 1.01
Weighted average common shares outstanding				
Basic	159.0	163.2	158.7	167.6
Diluted	160.2	166.2	159.8	170.6

See Notes to Condensed Consolidated Financial Statements.

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Condensed Consolidated Balance Sheets (Unaudited)

In millions, except per share amounts

	September 30, 2009	December 31, 2008
Assets		
Current assets		
Cash and cash equivalents	$ 419	$ 711
Accounts receivable, net	844	913
Inventories, net	708	692
Other current assets	270	241
Total current assets	2,241	2,557
Property, plant and equipment, net	345	308
Goodwill	89	84
Prepaid pension cost	230	251
Deferred income taxes	634	645
Other assets	365	410
Total assets	$ 3,904	$ 4,255
Liabilities and stockholders equity		
Current liabilities		
Short-term borrowings	$ -	$ 301
Accounts payable	532	492
Payroll and benefits liabilities	137	210
Deferred service revenue and customer deposits	344	317
Other current liabilities	313	373
Total current liabilities	1,326	1,693
Long-term debt	11	7
Pension and indemnity plan liabilities	1,494	1,424
Postretirement and postemployment benefits liabilities	339	359
Deferred income taxes	10	9
Income tax accruals	144	155
Other liabilities	101	143
Total liabilities	3,425	3,790
Commitments and contingencies (Note 8)		
Stockholders equity		
NCR stockholders equity		
Preferred stock: par value $0.01 per share, 100.0 shares authorized, no shares issued and outstanding at September 30, 2009 and December 31, 2008	-	-
	2	2

Common stock: par value $0.01 per share, 500.0 shares authorized, 159.2 and 158.1 shares issued and outstanding at September 30, 2009 and December 31, 2008, respectively				
Paid-in capital		263		248
Retained earnings		1,857		1,834
Accumulated other comprehensive loss		(1,672)		(1,644)
Total NCR stockholders equity		450		440
Noncontrolling interests in subsidiaries		29		25
Total stockholders equity		479		465
Total liabilities and stockholders equity	$	3,904	$	4,255

See Notes to Condensed Consolidated Financial Statements.

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Condensed Consolidated Statements of Cash Flows (Unaudited)

In millions

	Nine Months Ended September 30 2009	2008
Operating activities		
Net income	$ 27	$ 171
Adjustments to reconcile net income to net cash provided by operating activities:		
Loss from discontinued operations	-	4
Depreciation and amortization	92	83
Stock-based compensation expense	11	30
Excess tax benefit from stock-based compensation	-	(2)
Deferred income taxes	(30)	29
Gains on sale of property, plant and equipment	(5)	(28)
Impairment of equity investments	22	-
Changes in operating assets and liabilities:		
Receivables	71	224
Inventories	(12)	6
Current payables and accrued expenses	(62)	(140)
Deferred service revenue and customer deposits	27	5
Employee severance and pension	40	(21)
Other assets and liabilities	(65)	(54)
Net cash provided by operating activities	116	307
Investing activities		
Expenditures for property, plant and equipment	(68)	(58)
Proceeds from sales of property, plant and equipment	4	54
Additions to capitalized software	(46)	(47)
Other investing activities, business acquisitions and divestitures, net	(12)	(54)
Net cash used in investing activities	(122)	(105)
Financing activities		
Repurchases of Company common stock	(1)	(424)
Excess tax benefit from stock-based compensation	-	2
Repayment of senior unsecured notes	(300)	-
Payments on revolving credit facility	(30)	-
Borrowings on revolving credit facility	30	-
Proceeds from employee stock plans	6	15
Net cash used in financing activities	(295)	(407)
Cash flows from discontinued operations		
Net cash used in operating activities	-	(17)
Effect of exchange rate changes on cash and cash equivalents	9	3
Decrease in cash and cash equivalents	(292)	(219)

Cash and cash equivalents at beginning of period	711	952
Cash and cash equivalents at end of period	$ 419	$ 733

See Notes to Condensed Consolidated Financial Statements.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. BASIS OF PRESENTATION

The accompanying Condensed Consolidated Financial Statements have been prepared by NCR Corporation (NCR, the Company, we or us) without audit pursuant to the rules and regulations of the U.S. Securities and Exchange Commission (SEC) and, in the opinion of management, include all adjustments (consisting of normal recurring adjustments) necessary for a fair statement of the consolidated results of operations, financial position, and cash flows for each period presented. The consolidated results for the interim periods are not necessarily indicative of results to be expected for the full year. The year-end condensed balance sheet was derived from audited financial statements, but does not include all disclosures required by accounting principles generally accepted in the United States (GAAP). These financial statements should be read in conjunction with NCR s Form 10-K for the year ended December 31, 2008.

Use of Estimates GAAP requires management to make estimates and judgments that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and revenues and expenses during the period reported. Actual results could differ from those estimates.

Evaluation of Subsequent Events The Company evaluated subsequent events through October 30, 2009, the date our Condensed Consolidated Financial Statements were issued. No matters were identified that would materially impact our Condensed Consolidated Financial Statements or require disclosure in accordance with Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 855-10.

Out of Period Adjustments In the nine months ended September 30, 2009, the Company recorded adjustments to decrease product revenue by $10 million and cost of products by $7 million, which resulted in a net decrease in gross margin and net income of $3 million. The adjustments related to revenue incorrectly recorded during 2008 by the Company s Japanese subsidiary.

The Company determined that the impact of this error, was not material to the 2008 annual and interim financial statements and the effect of correcting this error in the nine months ended September 30, 2009 is not material to the expected 2009 annual financial statements.

2. SUPPLEMENTAL FINANCIAL INFORMATION

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In millions	Three Months Ended September 30 2009	2008	Nine Months Ended September 30 2009	2008
Comprehensive Income				
Income from continuing operations	**$ 17**	$ 82	**$ 27**	$ 175
Other comprehensive (loss) income, net of tax:				
Unrealized loss on securities	**(1)**	(2)	**-**	(4)
Unrealized gain on derivatives accounted for as hedges	**1**	4	**6**	3
Change to unrecognized losses and prior service cost related to pension, postemployment and postretirement benefits	**(15)**	(14)	**(52)**	16
Currency translation adjustments	**-**	(55)	**18**	(50)
Comprehensive income (loss) from continuing operations	**2**	15	**(1)**	140
Comprehensive loss from discontinued operations	**-**	(2)	**-**	(4)
Total comprehensive income (loss)	**2**	13	**(1)**	136
Comprehensive income attributable to noncontrolling interests	**4**	2	**4**	2
Comprehensive (loss) income attributable to NCR	**$ (2)**	$ 11	**$ (5)**	$ 134

The following table provides a reconciliation of total stockholders equity, stockholders equity attributable to NCR, and the noncontrolling interests for the nine months ended September 30, 2009 and September 30, 2008:

In millions	Total Stockholders Equity	Total Stockholders Equity Attributable to NCR	Noncontrolling Interests in Subsidiaries
December 31, 2007	$ 1,776	$ 1,757	$ 19
Net income (loss)	171	172	(1)
Other comprehensive (loss) income, net of tax:			
Currency translation adjustments	(50)	(53)	3
Unrealized losses on securities, net	(4)	(4)	-
Benefit plans, net	16	16	-
Unrealized gains on derivatives	3	3	-
Comprehensive income	136	134	2
Net share issuance and repurchase activity	(388)	(388)	-
September 30, 2008	$ 1,524	$ 1,503	$ 21
December 31, 2008	**$ 465**	**$ 440**	**$ 25**
Net income	**27**	**23**	**4**
Other comprehensive income (loss), net of tax:			
Currency translation adjustments	**18**	**18**	**-**
Unrealized gain on securities, net	**-**	**-**	**-**
Benefit plans, net	**(52)**	**(52)**	**-**
Unrealized gain on derivatives	**6**	**6**	**-**
Comprehensive (loss) income	**(1)**	**(5)**	**4**

Net share issuance and repurchase activity	**15**	**15**	**-**
September 30, 2009	**$ 479**	**$ 450**	**$ 29**

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In millions

	September 30, 2009	December 31, 2008
Inventories, net		
Work in process and raw materials	**$ 124**	$ 137
Finished goods	**192**	171
Service parts	**392**	384
Total inventories, net	**$ 708**	$ 692

3. NEW ACCOUNTING PRONOUNCEMENTS

Statement of Financial Accounting Standards No. 160 In December 2007, the FASB issued SFAS No. 160 (SFAS 160), *Noncontrolling Interests in Consolidated Financial Statements, an Amendment to ARB No.* 51. SFAS 160 applies to all entities that have an outstanding noncontrolling interest (formerly known as minority interest) in one or more subsidiaries or that deconsolidate a subsidiary. SFAS 160 is effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2008. The adoption of SFAS 160, effective January 1, 2009, did not have a material impact on the Company s Condensed Consolidated Financial Statements. In accordance with SFAS 160, which is now reflected at ASC 810-10, we have changed the presentation of our Condensed Consolidated Financial Statements, including the presentation of noncontrolling interests share of income or loss separately from net income attributable to NCR s common stockholders and the presentation of the noncontrolling interest within equity and have provided additional disclosures required by the standard in Note 2, Supplemental Financial Information .

FASB Staff Position No. FAS 157-2 In February 2008, the FASB issued FASB Staff Position No. FAS 157-2 (FSP 157-2), *Effective Date of FASB Statement No. 157,* which delayed the effective date for measuring nonfinancial assets and nonfinancial liabilities at fair value, except for items that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually). FSP 157-2 is now reflected at ASC 820-10 and the adoption of this guidance on January 1, 2009 did not have a material impact on the Company s Condensed Consolidated Financial Statements; however, we have provided additional disclosures as required by ASC 820-10 in Note 12, Fair Value of Assets and Liabilities .

Statement of Financial Accounting Standards No. 161 In March 2008, the FASB issued SFAS No. 161 (SFAS 161), *Disclosures about Derivative Instruments and Hedging Activities*. The additional disclosures required as a result of this guidance is intended to help investors better understand how derivative instruments and hedging activities affect an entity s financial position, financial performance and cash flows through enhanced disclosure requirements. SFAS 161, the guidance of which is now reflected at ASC 815-10-50 is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008. The adoption of ASC 815-10-50, effective January 1, 2009, did not have an impact on the Company s Condensed Consolidated Financial Statements; however, we have enhanced certain disclosures to comply with the new standard. See Note 15, Derivatives and Hedging Instruments for the additional disclosures.

FASB Staff Position No. FAS 142-3 In April 2008, the FASB issued FASB Staff Position No. 142-3 (FSP 142-3), *Determination of the Useful Life of Intangible Assets.* FSP 142-3 amends the factors that should be considered in developing renewal or extension assumptions used to determine the useful life of a recognized intangible asset under ASC 350-10 (prior authoritative guidance: SFAS No. 142, *Goodwill and Intangible Assets*). FSP 142-3, which is now reflected at ASC 805-10, is effective for fiscal years beginning after December 15, 2008. The adoption of this guidance, effective January 1, 2009, did not have an impact on the Company s Condensed Consolidated Financial Statements.

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Emerging Issues Task Force Issue 08-6 In November 2008, the EITF issued their final consensus for EITF Issue 08-6**,** *Equity Method Investment Accounting Considerations* (EITF 08-6), which provides guidance regarding certain matters related to the accounting for equity method investments, including the method of determining the initial carrying value of such investments, the method for measuring and recognizing other-than-temporary impairments, and the accounting for share issuance by investees. EITF 08-6 is now reflected at ASC 323-10. The adoption of this guidance, effective January 1, 2009, did not have an impact on the Company s Condensed Consolidated Financial Statements.

FASB Staff Position No. FAS 132(R)-1 In December 2008, the FASB issued FSP No. FAS 132(R)-1, *Employers Disclosures about Postretirement Benefit Plan Assets,* which requires additional disclosures by public companies regarding plan assets of defined benefit pension or other postretirement benefit plans. The FSP requires additional disclosures regarding the investment allocation decision making process, the fair value of each major category of plan assets, and the inputs and valuation techniques used to measure the fair value of the plan assets. The required disclosures are effective for fiscal years ending after December 15, 2009; however, early application is permitted. The disclosures will not be required for earlier periods presented for comparative purposes. We will adopt the guidance, which is now reflected at ASC 715-20, on its effective date and will report the required disclosures in our Form 10-K for the period ending December 31, 2009.

FASB Staff Position No. FAS 141(R)-1 In February 2009, the FASB issued FSP No. FAS 141(R)-1, *Accounting for Assets Acquired and Liabilities Assumed in a Business Combination That Arise from Contingencies*, which amends the provisions related to the initial recognition and measurement, subsequent measurement and disclosure of assets and liabilities arising from contingencies in a business combination under ASC 805-10 (prior authoritative guidance: SFAS No. 141(R), *Business Combinations*). The FSP applies to all assets acquired and liabilities assumed in a business combination that arise from contingencies that would be within the scope of ASC 450-10 (prior authoritative guidance: SFAS No. 5, *Accounting for Contingencies*), if not acquired or assumed in a business combination, except for assets or liabilities arising from contingencies that are subject to specific guidance at ASC 805-10. The FSP, which is now reflected at ASC 805-20, applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. The adoption of the FSP, effective January 1, 2009, did not have an impact on the Company s Condensed Consolidated Financial Statements.

FASB Staff Position No. FAS 115-2 and FAS 124-2 In April 2009, the FASB Issued FSP No. FAS 115-2 and FAS 124-2 (FSP 115-2/124-2), *Recognition and Presentation of Other-Than-Temporary Impairments*, which amends other-than-temporary impairment guidance in GAAP for debt securities to make the guidance more operational and improve the presentation and disclosure of other-than-temporary impairments of debt and equity securities in the financial statements. In cases where the amortized cost of a debt security exceeds its fair value, FSP 115-2/124-2 requires that an entity assess whether it has the intent to sell the debt security or whether it is more likely than not that it will be required to sell the debt security before the anticipated recovery of its amortized cost basis. If either of these conditions is met, the entity must recognize an other-than-temporary impairment. In addition, FSP 115-2/124-2 requires that an impairment be separated into the amount of the total impairment related to the credit loss and the amount of the impairment related to all other factors. The amount of the other-than-temporary impairment related to the credit loss is recognized in earnings, while the impairment related to all other factors is recognized in other comprehensive income. FSP 115-2/124-2 is effective for all interim and annual periods ending after June 15, 2009. The adoption of the FSP, which is now reflected at ASC 320-10, during the second quarter of 2009 did not have a material impact on the Company s financial position, results of operations or liquidity.

FASB Staff Position No. FAS 157-4 In April 2009, the FASB issued FSP No. 157-4 (FSP 157-4), *Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly*. FSP 157-4 provides additional guidance for estimating fair value in accordance with ASC 820-10 (prior authoritative guidance: SFAS No. 157, *Fair Value Measurements*) when the volume and level of activity for the asset or liability have significantly decreased and includes guidance on identifying circumstances that indicate a transaction is not orderly. FSP 157-4 is effective for all interim and annual periods ending after June 15, 2009. The adoption of the FSP, which is now reflected at ASC 820-10, during the second quarter of 2009 did not have a material impact on the Company s financial position, results of operations or liquidity.

FASB Staff Position No. FAS 107-1 and APB 28-1 In April 2009, the FASB issued FSP No. 107-1 and APB 28-1 (FSP 107-1 and 28-1), *Interim Disclosures about Fair Value of Financial Instruments*, which amends SFAS No. 107, *Disclosures about Fair Value of Financial Instruments*, to require disclosures about fair value of financial instruments for interim reporting periods of publicly traded companies as well as in annual financial statements. FSP 107-1 and 28-1 also amends APB Opinion No. 28, *Interim Financial Reporting*, to require those disclosures in summarized financial information at interim reporting periods. FSP 107-1 and 28-1, which is now reflected at ASC 825-10, is effective for interim reporting periods ending after June 15, 2009, with early adoption permitted for periods ending after March 15, 2009. The adoption of the FSP during the second quarter of 2009 did not have a material impact on the Company s Condensed Consolidated Financial Statements; however, we have provided additional disclosures as required by the FSP in Note 14, Debt Obligations .

Statement of Financial Accounting Standards No. 165 In May 2009, the FASB issued SFAS No. 165, which establishes general standards of accounting for and disclosure of events that occur after the balance sheet date, but before the financial statements are issued or available to be issued. SFAS 165,which is reflected at ASC 855-10 is effective for interim and annual reporting periods ending after June 15, 2009. The adoption of SFAS 165 during the second quarter of 2009 did not have an impact on the Company s financial position, results of operations or liquidity. We have provided the required disclosures in Note 1, Basis of Presentation .

Statement of Financial Accounting Standards No. 167 In June 2009, the FASB issued SFAS No. 167 (SFAS 167), *Amendments to FASB Interpretation No. 46(R)*, which amends ASC 810-10 to require ongoing reassessments of whether an enterprise is the primary beneficiary of a variable interest entity. In addition, SFAS 167 amends ASC 810-10 to eliminate the quantitative approach previously required for determining the primary beneficiary of a variable interest entity. SFAS 167 amends certain guidance at ASC 810-10 for determining whether an entity is a variable interest entity and adds an additional reconsideration event for determining whether an entity is a variable interest entity when any changes in facts and circumstances occur such that the holders of the equity investment at risk, as a group, lose the power from voting rights or similar rights to direct the activities of the entity that most significantly impact the entity s economic performance. Further, SFAS 167 requires enhanced disclosures that will provide users of financial statements with more transparent information about an enterprise s involvement in a variable interest entity. SFAS 167 is effective as of the beginning of the first annual reporting period and interim reporting periods that begin after November 15, 2009. The adoption of this guidance is not expected to have a material impact on the Company s financial position, results of operations or liquidity.

Statement of Financial Accounting Standards No. 168 In June 2009, the FASB issued SFAS No. 168 (SFAS 168), The FASB Accounting Standards Codification™ *and the Hierarchy of Generally Accepted Accounting Principles a replacement of FASB Statement No. 162.* In accordance with SFAS 168, the FASB Accounting Standards Codification™ (Codification) is the source of authoritative GAAP recognized by the FASB to be applied by nongovernmental entities. Rules and interpretive releases by the SEC under authority of federal securities laws are also sources of authoritative GAAP for SEC registrants.

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SFAS 168, which is reflected at ASC 105-10, is effective for financial statements issued for interim and annual periods ending after September 15, 2009. The adoption of this guidance did not have an impact on the Company s financial position, results of operations or liquidity; however, financial statement disclosures that refer to GAAP now provide references to the Codification rather than FASB Statements, FASB Staff Positions, or Emerging Issues Task Force Abstracts.

Emerging Issues Task Force Issue 08-1 In September 2009, the EITF issued their final consensus for EITF Issue 08-1 (EITF 08-1), *Revenue Arrangements with Multiple Deliverables*, which will supersede the guidance in ASC 605-25 (previous authoritative guidance: Issue 00-21, *Revenue Arrangements with Multiple Deliverables*). When vendor specific objective evidence or third party evidence of selling price for deliverables in an arrangement cannot be determined, NCR will be required to develop a best estimate of the selling price to separate deliverables and allocate arrangement consideration using the relative selling price method. Additionally, this guidance eliminates the residual method of allocation, which NCR has historically applied to certain customer arrangements. The new guidance is effective for fiscal years beginning after June 15, 2010. The Company is in the process of determining the effect of the adoption of the guidance in EITF 08-1.

Emerging Issues Task Force Issue 09-3 In September 2009, the EITF issued their final consensus for EITF Issue 09-3 (EITF 09-3), *Applicability of SOP 97-2 to Certain Arrangements that Include Software Elements,* which amends the prior guidance to exclude tangible products that contain software and non-software components that function together to deliver the products essential functionality from the guidance on software revenue recognition. The guidance is effective for fiscal years beginning after June 15, 2010; however, early adoption is permitted as of the beginning of an entity s fiscal year. Entities are required to adopt EITF 08-1 and EITF 09-3 concurrently. The Company is in the process of determining the effect of the adoption of the guidance in this EITF.

4. REALIGNMENT ACTIVITIES AND REAL ESTATE TRANSACTIONS

Organizational Realignment On January 1, 2008, NCR began management of its business on a geographic basis, changing from a previous model of global business units organized by product and service offering. As a result, in the second quarter of 2008, NCR commenced a global realignment initiative to reduce redundancies and process inefficiencies to become more customer-focused and market-driven. This initiative is addressing legacy process inefficiencies and unbalanced resource allocation by focusing on organizational design, process re-engineering and business process outsourcing. The initiative has resulted in reductions in employment and productivity improvements, while freeing up funds to invest in growth programs such as sales, engineering, and market development. The realignment activities included approximately 900 employee terminations and relate to each of our reportable segments of the Americas; Europe, Middle East and Africa (EMEA); and Asia Pacific and Japan (APJ).

The Company made $21 million in severance payments during the first nine months of 2009. As of September 30, 2009, there was a remaining accrued liability of $3 million as compared to $26 million as of December 31, 2008. This liability is recorded in the Condensed Consolidated Balance Sheet in other current liabilities as the Company expects that payment of the remaining obligation will occur in the fourth quarter of 2009.

The actions taken to date are expected to generate incremental, annualized savings of approximately $40 million. We realized approximately half of that amount during 2008 and will achieve the full, annualized savings beginning in 2009. The Company continues to identify additional opportunities focusing on organizational design, process re-engineering and business process outsourcing and therefore, expects additional realignment activities through 2010 as a result of this initiative. The costs and related savings from these additional activities are not reasonably estimable at this time as we are in the process of defining the scope of the activities and quantifying the impacts thereof.

Manufacturing Realignment In the first quarter of 2007, the Company initiated a manufacturing realignment initiative primarily related to its ATM products, which included outsourcing certain manufacturing activities in the Americas region and shifting other manufacturing activities from high cost to low cost geographies in the

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EMEA region as well as the APJ region. This realignment resulted in approximately 1,100 employee terminations and, as expected, improved productivity and freed capital in order to invest the related cost savings in revenue-generating programs such as sales, engineering and market development. During the second quarter of 2009, the Company released the remaining $1 million reserve related to the manufacturing realignment due to changes in estimates of remaining severance payments and recorded this amount as a reduction in cost of products in the Condensed Consolidated Statement of Operations.

The following table summarizes the total liabilities for these realignment activities, which are included on the Condensed Consolidated Balance Sheets in other current liabilities.

In millions	2008 Organizational Realignment	2007 Manufacturing Realignment	Total
Employee Severance and Other Benefits			
Balance as of January 1, 2009	**$ 26**	**$ 1**	**$ 27**
Foreign currency translation adjustments	**(2)**	**-**	**(2)**
Payments made during the nine months ended September 30, 2009	**(21)**	**-**	**(21)**
Changes in estimates during the nine months ended September 30, 2009	**-**	**(1)**	**(1)**
Ending balance as of September 30, 2009	**$ 3**	**$ -**	**$ 3**

Real estate consolidation and restructuring During the nine months ended September 30, 2008, the Company recognized $28 million in gains from the sale of property, plant, and equipment in the Condensed Consolidated Statement of Operations. Of this amount, $23 million related to the sale of two properties in Canada and was recorded as a reduction to selling, genen="bottom">
Primary residential

Revenues
$4,622 $5,536
Expenses
6,264 7,434

Segment operating loss
(1,642) (1,898)

Active adult communities

Revenues
4,678 6,198
Expenses
6,691 7,630

Segment operating loss
(2,013) (1,432)

Commercial and industrial and other land sales

Revenues
1,825
Expenses
37 47

Segment operating income (loss)
(37) 1,778

Other operations

Revenues
191 228
Expenses
200 217

Segment operating loss
(9) 11

Operating income (loss)
(3,701) (1,541)

Unallocated income (expenses):

Interest income
122 199
Gain on repurchase of 4.50% Notes
1,365
Equity loss from unconsolidated entities
(90) (62)
Net loss attributable to non-controlling interests
133
General and administrative expenses
(4,083) (4,667)
Interest expense
(1,676) (1,837)
Other real estate expenses
(841) (2,563)
Impairment of the Poinciana Parkway
(318)

Loss before income taxes
(10,136) (9,424)
Income tax benefit
830

Net loss
($10,136) ($8,594)

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Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations (dollars in thousands except share and per share data) continued

RESULTS OF OPERATIONS continued

Data from closings for the primary residential and active adult homebuilding segments for the three months ended March 31, 2010 and 2009 is summarized as follows:

For the three months ended March 31,	Number of Units	Revenues	Average Price Per Unit
2010			
Primary residential	20	$ 3,931	$ 197
Active adult communities	8	1,520	$ 190
Total	28	$ 5,451	$ 195
2009			
Primary residential	22	$ 4,684	$ 213
Active adult communities	12	3,071	$ 256
Total	34	$ 7,755	$ 228

Data from contracts signed for the primary residential and active adult homebuilding segments for the three months ended March 31, 2010 and 2009 is summarized as follows:

For the three months ended March 31,	Gross Number of Contracts Signed	Cancellations	Contracts Signed, Net of Cancellations	Dollar Value	Average Price Per Unit
2010					
Primary residential	20	(4)	16	$ 2,865	$ 179
Active adult communities	47	(3)	44	9,289	$ 211
Total	67	(7)	60	$ 12,154	$ 203
2009					
Primary residential	48	(9)	39	$ 6,951	$ 178
Active adult communities	23	(5)	18	3,387	$ 188
Total	71	(14)	57	$ 10,338	$ 181

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RESULTS OF OPERATIONS continued

Backlog for the primary residential and active adult homebuilding segments as of March 31, 2010 and 2009 is summarized as follows:

As of March 31,	Number of Units	Dollar Volume	Average Price Per Unit
2010			
Primary residential	12	$ 2,157	$ 180
Active adult communities	45	10,015	$ 223
Total	57	$ 12,172	$ 214
2009			
Primary residential	33	6,868	$ 208
Active adult communities	46	11,793	$ 256
Total	79	$ 18,661	$ 236

The number of net housing contracts signed during the three months ended March 31, 2010 compared to the same period in 2009 increased 5.3% and the dollar value of housing contracts signed increased 17.6%, including 28 sales contracts representing an aggregate dollar value of approximately $4,377 in Seasons at Tradition. The low volume of housing contracts signed for the three months ended March 31, 2010 continues to reflect the weak market for new residences in the geographic areas where our communities are located. Our communities are located in areas of Florida and Arizona where there is an excess of units for sale, including foreclosures and assets being sold by lenders, and continued use of various sales incentives by residential builders in our markets, including Avatar. During the three months ended March 31, 2010, cancellations of previously signed contracts totaled 7 compared to 14 during the three months ended March 31, 2009. As a percentage of the gross number of contracts signed, this represents 10% and 20%, respectively.

As of March 31, 2010, our inventory of unsold (speculative) homes, both completed and under construction, was 122 units compared to 144 units as of December 31, 2009. As of March 31, 2010, approximately 79% of unsold homes were completed compared to approximately 83% as of December 31, 2009.

During the three months ended March 31, 2010 compared to the three months ended March 31, 2009, the number of homes closed decreased by 17.6%, from 34 to 28, and the related revenues decreased by 29.7%, from $7,755 to $5,451. Our average sales price for homes closed during the three months ended March 31, 2010 declined to $195 compared to $228 for the three months ended March 31, 2009. We anticipate that we will close in excess of 80% of the homes in backlog as of March 31, 2010 during the subsequent 12-month period, subject to cancellations by purchasers prior to scheduled delivery dates. We do not anticipate a meaningful improvement in our markets in the near term.

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RESULTS OF OPERATIONS continued

Net loss for the three months ended March 31, 2010 and 2009 was ($10,136) or ($0.90) per basic and diluted share and ($8,594) or ($0.99) per basic and diluted share, respectively. The increase in net loss for the three months ended March 31, 2010 compared to the same period in 2009 was primarily due to decreased pre-tax profits from commercial and industrial and other land sales as well as increased losses from our primary residential and active adult operations. In addition, the increase in pre-tax loss for the three months ended March 31, 2010 compared to the same period in 2009 was partially due to the pre-tax gain on the repurchase of the 4.50% Notes in 2009.

Revenues from primary residential operations decreased $914, or 16.5%, for the three months ended March 31, 2010 compared to the same period in 2009. Expenses from primary residential operations decreased $1,170, or 15.7%, for the three months ended March 31, 2010 compared to the same period in 2009. The decrease in revenues is primarily attributable to decreased closings and average sales prices in our primary residential homebuilding communities. The decrease in expenses is attributable to lower volume of closings. During the three months ended March 31, 2010 and 2009, we recorded impairment charges in our primary residential operations of approximately $168 and $373, respectively, from homes completed or under construction. The average sales price on closings from primary residential homebuilding operations for the three months ended March 31, 2010 was $197 compared to $213 for the same period in 2009. The average contribution margin (excluding impairment charges) on closings from primary residential homebuilding operations for the three months ended March 31, 2010 was approximately (5%) compared to approximately 8% for the same period in 2009. Included in the results from primary residential operations are divisional overhead not specifically allocated to specific communities and our amenity operations. We have been experiencing increased defaults in payments of club dues for our amenities compared to previous years.

Revenues from active adult operations decreased $1,520, or 24.5%, for the three months ended March 31, 2010 compared to the same period in 2009. Expenses from active adult operations decreased $939, or 12.3%, for the three months ended March 31, 2010 compared to the same period in 2009. The decrease in revenues is primarily attributable to decreased closings and average sales prices. The decrease in expenses is attributable to lower volume of closings partially offset by expenditures incurred during the first quarter of 2010 for the recently acquired Seasons at Tradition. The average sales price on closings from active adult homebuilding operations for the three months ended March 31, 2010 was $190 compared to $256 for the same period in 2009. The average contribution margin (excluding impairment charges) on closings from active adult homebuilding operations for the three months ended March 31, 2010 was approximately 4% compared to approximately 19% for the same period in 2009. Included in the results from active adult operations are divisional overhead not specifically allocated to specific communities and our amenity operations. We have been experiencing increased defaults in payments of club dues for our amenities compared to previous years.

The amount and types of commercial and industrial and other land sold vary from year to year depending upon demand, ensuing negotiations and the timing of the closings of these sales. During the three months ended March 31, 2010, we did not have sales of commercial, industrial and other land. During the three months ended March 31, 2009, pre-tax profits from sales of commercial, industrial and other land were $1,778 on revenues of $1,825.

For the three months ended March 31, 2009, pre-tax profits from commercial and industrial land were $1,758 on aggregate revenues of $1,785. For the three months ended March 31, 2009, pre-tax profits from other land sales were $20 on aggregate revenues of $40.

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RESULTS OF OPERATIONS continued

Revenues from other operations decreased $37, or 16.2%, for the three months ended March 31, 2010 compared to the same period in 2009. Expenses from other operations decreased $17, or 7.8%, for the three months ended March 31, 2010 compared to the same period in 2009. The decreases in revenues and expenses are primarily attributable to decreased operating results from our title insurance agency operations due to lower volume of real estate transactions.

Interest income decreased $77, or 38.7%, for the three months ended March 31, 2010 compared to the same period in 2009. The decrease was primarily attributable to decreased interest rates earned on our cash and cash equivalents during 2010 as compared to 2009.

During the three months ended March 31, 2009, we repurchased $7,500 principal amount of the 4.50% Notes for approximately $6,038 including accrued interest. This repurchase resulted in a pre-tax gain during the first quarter of 2009 of approximately $1,365, which is included in Other Revenues in the consolidated statements of operations for the three months ended March 31, 2009 including the write-off of approximately $63 of deferred finance costs.

General and administrative expenses decreased $584, or 12.5%, for the three months ended March 31, 2010 compared to the same period in 2009. The decrease was primarily due to decreases in compensation expense, share-based compensation expense and professional fees.

Interest expense decreased $161, or 8.8%, for the three months ended March 31, 2010 compared to the same period in 2009. The decrease in interest expense is primarily attributable to the decrease in outstanding indebtedness during 2010 compared to 2009, as a result of our repurchase of 4.50% Notes.

Other real estate expenses, net, represented by real estate taxes, property maintenance and miscellaneous income not allocable to specific operations, decreased by $1,722, or 67.2%, for the three months ended March 31, 2010 compared to the same period in 2009. The decrease is primarily attributable to the reduction in charges related to the required utilities improvements of more than 8,000 residential homesites in Poinciana and Rio Rico substantially sold prior to the termination of the retail homesite sales programs in 1996. During the three months ended March 31, 2010 and 2009, we recognized charges of $0 and $545, respectively. These charges were based on third-party engineering evaluations. Future increases or decreases of costs for construction, material and labor as well as other land development and utilities infrastructure costs may have a significant effect on the estimated development liability. Also contributing to the decrease in other real estate expenses for the three months ended March 31, 2010 and 2009 are non-capitalizable expenditures of $208 and $341, respectively, related to the Poinciana Parkway.

The income tax benefit of $830 for the three months ended March 31, 2009 was due to an adjustment to reduce the valuation allowance to reflect the tax effect of certain restricted stock compensation expense for which the tax deduction was taken in 2008 and is also reflected as a decrease in additional paid-in capital. In accordance with ASC 740, we evaluate our deferred tax assets quarterly to determine if valuation allowances are required. ASC 740 requires that companies assess whether valuation allowances should be established based on the consideration of all available evidence using a more likely than not standard. During 2008, we established a valuation allowance against our deferred tax assets. Our cumulative loss position over the evaluation period and the uncertain and volatile market conditions provided significant evidence supporting the need for a valuation allowance. During the three months ended March 31, 2010 we recognized an increase of $3,882 in the valuation allowance. As of March 31, 2010, our deferred tax asset valuation allowance was $14,301. In future periods, the allowance could be reduced based on sufficient evidence indicating that it is more likely than not that a portion of our deferred tax assets will be realized.

Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations (dollars in thousands except share and per share data) continued

LIQUIDITY AND CAPITAL RESOURCES

Our primary business activities are capital intensive in nature. Significant capital resources are required to finance planned primary residential and active adult communities, homebuilding construction in process, community infrastructure, selling expenses, new projects and working capital needs, including funding of debt service requirements, operating deficits and the carrying costs of land.

With the deterioration in the residential land and housing values in Florida and Arizona, we are focused on maintaining sufficient liquidity. As of March 31, 2010, our cash and cash equivalents totaled $213,233. As of March 31, 2010, we had borrowings of $55,842 outstanding under the Amended Unsecured Credit Facility, and the principal amount of the 4.50% Notes outstanding was $64,804.

Our operating cash flows fluctuate relative to the status of development within existing communities, expenditures for land, new developments and other real estate activities, and sales of various homebuilding product lines within those communities and other developments.

For the three months ended March 31, 2010, net cash used in operating activities amounted to $3,870, primarily to fund our operating losses. Net cash provided by investing activities amounted to $10 due to a refund received from previous expenditures of $30 on the Poinciana Parkway offset by expenditures of $20 for investments in property and equipment. Net cash used by financing activities of $39 was attributable to payment of principal under the Amended Unsecured Credit Facility.

For the three months ended March 31, 2009, net cash used in operating activities amounted to $2,834, primarily to fund our operating losses. Net cash used in investing activities amounted to $107 as a result of expenditures of $77 for investments in property and equipment, expenditures of $7 on the Poinciana Parkway and investment in unconsolidated entities of $23. Net cash used by financing activities of $25 was attributable to payment of principal under the Amended Unsecured Credit Facility.

In 2006, we closed on substantially all of the land sold under the threat of condemnation, and in 2007 we closed on the remainder. We believe these transactions entitled us to defer the payment of income taxes of $24,355 from the gain on these sales. During October 2009, we received from the Internal Revenue Service a final extension until December 31, 2010 to obtain replacement property to defer the entire payment of income taxes. It is our intention to acquire replacement property by December 31, 2010. It is possible that we may not identify and purchase adequate replacement property within the required time period, which would require us to make this income tax payment plus interest of approximately $7,000 as of December 31, 2010.

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LIQUIDITY AND CAPITAL RESOURCES continued

As of March 31, 2010, the amount of our borrowings totaled $119,322 compared to our borrowings of $119,002 as of December 31, 2009. At March 31, 2010, our borrowings of $119,322 consisted of $63,369 carrying amount of the 4.50% Notes, $55,842 outstanding under the Amended Unsecured Credit Facility and $111 of 5.50% community development district term bond obligations due 2010.

On March 30, 2004, we issued $120,000 aggregate principal amount of the 4.50% Notes in a private offering. Interest is payable semiannually on April 1 and October 1. The 4.50% Notes are senior, unsecured obligations and rank equal in right of payment to all of our existing and future unsecured and senior indebtedness. However, the 4.50% Notes are effectively subordinated to all of our existing and future secured debt to the extent of the collateral securing such indebtedness, and to all existing and future liabilities of our subsidiaries.

Each $1 in principal amount of the 4.50% Notes is convertible, at the option of the holder, at a conversion price of $52.63, or 19.0006 shares of our common stock, upon the satisfaction of one of the following conditions: a) during any calendar quarter (but only during such calendar quarter) commencing after June 30, 2004 if the closing sale price of our common stock for at least 20 trading days in a period of 30 consecutive trading days ending on the last trading day of the preceding calendar quarter is more than 120% of the conversion price per share of common stock on such last day; or b) during the five business day period after any five-consecutive-trading-day period in which the trading price per $1 principal amount of the 4.50% Notes for each day of that period was less than 98% of the product of the closing sale price for our common stock for each day of that period and the number of shares of common stock issuable upon conversion of $1 principal amount of the 4.50% Notes, provided that if on the date of any such conversion that is on or after April 1, 2019, the closing sale price of Avatar s common stock is greater than the conversion price, then holders will receive, in lieu of common stock based on the conversion price, cash or common stock or a combination thereof, at our option, with a value equal to the principal amount of the 4.50% Notes plus accrued and unpaid interest, as of the conversion date. The closing price of Avatar s common stock exceeded 120% ($63.156) of the conversion price for 20 trading days out of 30 consecutive trading days as of the last trading day of the fourth quarter of 2006, as of the last trading day of the first quarter of 2007 and as of the last trading day of the second quarter of 2007. Therefore, the 4.50% Notes became convertible for the quarter beginning January 1, 2007, for the quarter beginning April 1, 2007 and for the quarter beginning July 1, 2007. During 2008, 2009 and the first quarter of 2010, the closing price of Avatar s common stock did not exceed 120% ($63.156) of the conversion price for 20 trading days out of 30 consecutive trading days; therefore, the 4.50% Notes were not convertible during 2008, 2009 and the first quarter of 2010. During 2007, $200 principal amount of the 4.50% Notes were converted into 3,800 shares of Avatar common stock. During 2007, Avatar repurchased $5,000 principal amount of the 4.50% Notes for approximately $4,984 including accrued interest. During 2008, we repurchased $35,920 principal amount of the 4.50% Notes for approximately $28,112 including accrued interest. On March 30, 2009, we repurchased $7,500 principal amount of the 4.50% Notes for approximately $6,038 including accrued interest. This repurchase resulted in a pre-tax gain of approximately $1,365 (which is included in Other Revenues in the consolidated statements of operations for the three months ended March 31, 2009). On June 19, 2009, we repurchased $6,576 principal amount of the 4.50% Notes for approximately $5,658, including accrued interest. As of March 31, 2010, $64,804 principal amount of the 4.50% Notes remain outstanding.

We may, at our option, redeem for cash all or a portion of the 4.50% Notes at any time on or after April 5, 2011. Holders may require us to repurchase the 4.50% Notes for cash on April 1, 2011, April 1, 2014 and April 1, 2019; or in certain circumstances involving a designated event, as defined in the indenture for the 4.50% Notes, holders may require us to purchase all or a portion of their 4.50% Notes. In each case, we will pay a repurchase price equal to 100% of their principal amount, plus accrued and unpaid interest, if any.

Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations (dollars in thousands except share and per share data) continued

LIQUIDITY AND CAPITAL RESOURCES continued

Financial Accounting Standards Board (FASB) ASC Subtopic 470-20, *Debt with Conversion Options Cash Conversion* (ASC 470-20), requires the issuer of certain convertible debt instruments that may be settled in cash on conversion to separately account for the liability (debt) and equity (conversion option) components of the instrument in a manner that reflects the issuer s nonconvertible debt borrowing rate. ASC 470-20 requires bifurcation of the instrument into a debt component that is initially recorded at fair value and an equity component. The difference between the fair value of the debt component and the initial proceeds from issuance of the instrument is recorded as a component of equity. The excess of the principal amount of the liability component over its carrying amount and the debt issuance costs are amortized to interest cost using the interest method over the expected life of a similar liability that does not have an associated equity component.

As of March 31, 2010 and December 31, 2009, the 4.50% Notes and the equity component associated with the 4.50% Notes were comprised of the following:

	March 31, 2010	December 31, 2009
4.50% Notes		
Principal amount	$ 64,804	$ 64,804
Unamortized discount	(1,435)	(1,794)
Net carrying amount	$ 63,369	$ 63,010
Equity Component, net of income tax benefit	$ 13,737	$ 13,737

The discount on the liability component of the 4.50% Notes is amortized using the effective interest method based on an effective rate of 7.5%, which is the estimated market interest rate for similar debt without a conversion option on the issuance date. The discount is amortized from the issuance date in 2004 through April 1, 2011, the first date that holders of the 4.50% Notes can require us to repurchase the 4.50% Notes. As of March 31, 2010, the remaining expected life over which the unamortized discount will be recognized is 1.0 year. We recognized $359 and $485 in non-cash interest charges related to the amortization of the discount during the three months ended March 31, 2010 and 2009, respectively.

On March 27, 2008, we entered into an Amended and Restated Credit Agreement, by and among our wholly-owned subsidiary, Avatar Properties Inc., as borrower, Wachovia Bank, National Association (as a lender and as administrative agent on behalf of the lenders), and certain financial institutions as lenders (the Amended Unsecured Credit Facility). This agreement amended and restated the Credit Agreement, dated as of September 20, 2005, as amended.

On May 3, 2010, we paid in full the outstanding principal and accrued interest of $55,979 under our Amended and Restated Credit Agreement. In addition, on May 4, 2010, we deposited $22,035 with Wells Fargo, N.A., successor by merger with Wachovia Bank, N.A., to secure the retirement of letters of credit outstanding under the credit facility. In connection with such payment and deposit, we notified our administrative agent that we were exercising our right to reduce our commitment amount under the facility to zero dollars ($0), which has the effect of terminating all parties obligations under the credit facility, effective no later than May 17, 2010. As of May 4, 2010, we had unrestricted cash and cash equivalents of approximately $161,000 and restricted cash of $22,035 deposited as security for the letters of credit.

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LIQUIDITY AND CAPITAL RESOURCES continued

As of March 31, 2010, the principal terms of the Amended Unsecured Credit Facility were as follows:

the amount of the facility was $100,000 (the facility was expandable up to $150,000, subject to certain conditions and lender approval);

financing for the Poinciana Parkway was permitted up to $140,000, subject to certain conditions;

certain covenants included: (i) the minimum adjusted EBITDA/Debt Service ratio (as defined) was 2.0, and provided for an alternative requirement of maintaining a maximum leverage ratio and minimum liquidity level if the minimum adjusted EBITDA/Debt Service ratio could not be maintained; (ii) the Leverage Ratio (as defined) was 1.75, and allowed us to net unrestricted cash in excess of $35,000 against outstanding debt in determining total liabilities; and (iii) we had no financial covenant as to the number of speculative homes and models if we maintained a Leverage Ratio (as defined) of 1.0 or less, however, if our Leverage Ratio exceeded 1.0, the number of speculative homes and models could not exceed 35% of unit closings for the trailing twelve month period; and

the pricing of the facility included: (i) the LIBOR Margin was a range of 2.0% to 2.75%, and depended on our EBITDA/Debt Service ratio, our rate on outstanding borrowings could have been increased up to an additional 50 basis points; (ii) our fee for outstanding letters of credit was 50 basis points below our LIBOR Margin; and (iii) our unused fee was a range of 25 basis points to 50 basis points, depending on our usage.

On November 7, 2008, Franklin Bank SSB (Franklin Bank), one of the participating financial institutions in our amended unsecured credit facility, was closed by the Texas Department of Savings and Mortgage Lending and the Federal Deposit Insurance Corporation (FDIC) was named receiver. On January 13, 2010, we received notification from the FDIC that Franklin Bank is no longer a participant in our amended unsecured credit facility. Franklin Bank was a 20% participant thus the principal amount of the Amended Unsecured Credit Facility is reduced to $80,000.

The Amended Unsecured Credit Facility included a $50,000 sublimit for the issuance of standby letters of credit. The maturity date of the Amended Unsecured Credit Facility was September 20, 2010. As of March 31, 2010, we had borrowings of approximately $55,842 outstanding under the Amended Unsecured Credit Facility and had letters of credit totaling $22,351 of which $20,869 were financial/maintenance letters of credit and $1,482 was a performance letter of credit. Under the Amended Unsecured Credit Facility, performance letters of credit did not count against our availability for borrowing. Our borrowing rate under the Amended Unsecured Credit Facility was 2.75% as of March 31, 2010. Our availability was approximately $3,289 as of March 31, 2010.

Also on March 27, 2008, in connection with the Amended Unsecured Credit Facility, Avatar Holdings Inc., as guarantor, entered into a Second Restated Guaranty Agreement with Wachovia Bank, National Association (as administrative agent and lender), in favor of certain financial institutions as lenders (Second Restated Guaranty Agreement). This agreement amended and restated the Restated Guaranty Agreement, dated as of October 21, 2005. Payments of all amounts due under the Amended Unsecured Credit Facility were guaranteed by Avatar Holdings Inc. pursuant to the Second Restated Guaranty Agreement.

Under the terms of the Amended Unsecured Credit Facility, we were required, among other things, to maintain a Minimum Tangible Net Worth (as defined) and certain financial covenant ratios. The Minimum Tangible Net Worth was increased quarterly by 25% of positive net income for the most recently ended fiscal quarter and 75% of the aggregate proceeds from any equity offerings during the most recently ended fiscal quarter. There was no decrease when we had net losses. As of March 31, 2010, our Minimum Tangible Net Worth requirement was $292,174.

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LIQUIDITY AND CAPITAL RESOURCES continued

Financial covenant ratios required under the Amended Unsecured Credit Facility consisted of maintaining at the end of each fiscal quarter a Leverage Ratio (as defined) of not more than 1.75 to 1, 1.50 to 1, 1.25 to 1, or 1.00 to 1; an Adjusted EBITDA/Debt Service Ratio (as defined) that was equal to or greater than 2.00 to 1; and a Notes Coverage Ratio (as defined) that was greater than or equal to 2.00 to 1.

If we did not meet the minimum required Adjusted EBITDA/Debt Service Ratio, we could alternatively comply by maintaining a reduced maximum Leverage Ratio and a minimum ACFFO (Adjusted Cash Flow from Operations, as defined) Ratio or Liquidity (as defined) requirement. The AFFCO Ratio requirement was greater than or equal to 1.50 to 1. If we did not meet the minimum required Adjusted EBITDA/Debt Service Ratio and ACFFO Ratio requirement, we could alternatively comply with a minimum Liquidity requirement of $50,000 (of which $25,000 is cash) when the EBITDA/Debt Service Ratio was greater than or equal to 1.00 to 1 and the Leverage Ratio was less than or equal to 1.25 to 1 or we could alternatively comply with a minimum Liquidity requirement of $75,000 (of which $35,000 is cash) when the EBITDA/Debt Service Ratio was less than 1.00 to 1 and the Leverage Ratio was less than or equal to 1.00 to 1.

The Amended Unsecured Credit Facility also contained limitations on investments relating to real estate related joint ventures; and restrictions on raw land, land under development and developed lots. Investments relating to real estate related joint ventures could not exceed 25% of Tangible Net Worth (as defined). The net book value of raw land, land under development and developed lots could not exceed 150% of Tangible Net Worth.

As of March 31, 2010, we were in compliance with the covenants of the Amended Unsecured Credit Facility.

The following summarizes certain financial covenant thresholds and our results pursuant to the Amended Unsecured Credit Facility as of March 31, 2010:

Financial Covenant	Covenant Requirement	Actual
Minimum Tangible Net Worth	$ 292,174	$ 435,131
Leverage Ratio (a)	Less than or equal to 1.00	(0.03)
EBITDA/Debt Service Ratio	(b)	(b)
AFFCO Ratio	(b)	(b)
Liquidity/Cash Requirements	$75,000/$35,000	$216,522/$213,233
Notes Coverage Ratio	Greater than or equal to 2.00	4.2
Investments in real estate related joint ventures (as a percent of Tangible Net Worth)	Less than or equal to 25%	1.2%
Book value of raw land, land under development and developed lots (as a percent of Tangible Net Worth)	Less than or equal to 150%	53%

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LIQUIDITY AND CAPITAL RESOURCES continued

(a) The Leverage Ratio requirement varies based on our Adjusted EBITDA/Debt Service Ratio. If our Adjusted EBITDA/Debt Service Ratio was greater than or equal to 2.00 to 1, the Leverage Ratio requirement was less than or equal to 1.75 to 1. If our Adjusted EBITDA/Debt Service Ratio was greater than or equal to 1.50 to 1, the Leverage Ratio requirement was less than or equal to 1.50 to 1. If our Adjusted EBITDA/Debt Service Ratio was greater than or equal to 1.00 to 1, the Leverage Ratio requirement was less than or equal to 1.25 to 1. If our Adjusted EBITDA/Debt Service Ratio was less than 1.00 to 1, the Leverage Ratio requirement was less than or equal to 1.00 to 1.

(b) Our Adjusted EBITDA/Debt Service Ratio of negative 5.5 was less than 1.00 to 1 as of March 31, 2010. Our AFFCO Ratio of 3.2 was more than 1.50 to 1 as of March 31, 2010. We were required to maintain Liquidity of $75,000 of which $35,000 was cash and cash equivalents.

Performance bonds, issued by third party entities, are used primarily to guarantee our performance to construct improvements in our various communities. As of March 31, 2010, we had outstanding performance bonds of approximately $3,011. We do not believe that it is likely any of these outstanding performance bonds will be drawn upon.

In conjunction with the acquisition of developed land in Florida in September 2005 and September 2004, we assumed approximately $5,900 of Community Development District term bond obligations due 2010. These term bonds are secured by the land and bear an interest rate of 5.50%. As of March 31, 2010, we had $111 outstanding under these obligations.

On October 13, 2008, our Board of Directors amended its June 2005 authorization to purchase the 4.50% Notes and/or common stock to allow expenditures up to $30,000, including the $9,864 previously authorized. On October 17, 2008, we repurchased $35,920 principal amount of the 4.50% Notes for approximately $28,112 including accrued interest. On December 12, 2008, our Board of Directors amended its June 2005 authorization to purchase the 4.50% Notes and/or common stock to allow expenditures up to $30,000, including the $1,888 remaining after the October 2008 activities. On March 30, 2009, we repurchased $7,500 principal amount of the 4.50% Notes for approximately $6,038 including accrued interest. On June 19, 2009, we repurchased $6,576 principal amount of the 4.50% Notes for approximately $5,658 including accrued interest. As of March 31, 2010, the remaining authorization is $18,304.

In December 2006, we entered into agreements with Osceola County, Florida and Polk County, Florida for us to develop and construct at our cost a 9.66 mile four-lane road in Osceola and Polk Counties, to be known as the Poinciana Parkway (the Poinciana Parkway). The Poinciana Parkway is to include a 4.15 mile segment to be operated as a toll road. We have acquired right-of-way and federal and state environmental permits necessary to construct the Poinciana Parkway. In July 2008 and August 2008, we entered into amended and restated agreements with Osceola County and Polk County, pursuant to which construction is to be commenced by February 14, 2011. Construction was to be completed by December 31, 2011 subject to extension for Force Majeure. We have notified the Counties that the completion date has been extended to October 14, 2013 due to Force Majeure related to the economic downturn. We advised the Counties that the current economic downturn has resulted in our inability to: (i) conclude negotiations with potential investors; or (ii) obtain financing for the construction of the Poinciana Parkway.

If funding for the Poinciana Parkway is not obtained and construction of the Poinciana Parkway cannot be commenced by February 14, 2011 as required by our agreements with Osceola County and Polk County, the Counties have no right to obtain damages or sue Avatar for specific performance. Polk County s sole remedy under its agreement with Avatar is to cancel such agreement if Avatar does not construct the Poinciana Parkway. If the construction of the Parkway is not funded and commenced by February 14, 2011, (i) a portion of Avatar s land in Osceola County will become subject to Osceola traffic concurrency requirements applicable generally to other home builders in the County and (ii) Avatar will be required to contribute approximately $1,900 towards the construction cost of certain traffic improvements in Osceola County that it otherwise might have been obligated to build or fund if it had not agreed to construct the Poinciana Parkway. Avatar is investigating the availability of an extension of the Poinciana Parkway permits and the related deadlines in its agreements with the Counties.

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Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations (dollars in thousands except share and per share data) continued

LIQUIDITY AND CAPITAL RESOURCES continued

Osceola County and Avatar were unsuccessful in their attempt to obtain a federal grant for construction of the Parkway. Osceola County and Avatar are still attempting to obtain other federal funds for development of the Poinciana Parkway, including highway tax bill monies, a newly announced federal transportation grant and a federal loan. We cannot predict whether any federal funds will be available.

For the Poinciana Parkway, indicators of impairment are general economic conditions, rate of population growth and estimated change in traffic levels. If indicators are present, we perform an impairment test in which the asset is reviewed for impairment by comparing the estimated future undiscounted cash flows to be generated by the asset to its carrying value. If such cash flows are less than the asset s carrying value, the carrying value is written down to its estimated fair value. In determining estimated future cash flows for purposes of the impairment test, we incorporate current market assumptions based on general economic conditions such as anticipated estimated revenues and estimated costs. These assumptions can significantly affect our estimates of future cash flows.

Our estimate of the right-of-way acquisition, development and construction costs for the Poinciana Parkway approximates $175,000 to $200,000. However, no assurance of the ultimate costs can be given at this stage. Of that amount approximately $47,000 has been expended as of March 31, 2010. During fiscal years 2008 and 2009 we recorded cumulative impairment charges of $38,336, associated with the Poinciana Parkway.

We review the recoverability of the carrying value of the Poinciana Parkway on a quarterly basis in accordance with authoritative accounting guidance. Based on our review as of March 31, 2010, we determined the estimated future undiscounted cash flows of the Poinciana Parkway were greater than its carrying value, therefore no impairment losses were recorded during the three months ended March 31, 2010. During the three months ended March 31, 2009, we recognized impairment losses of $318. In addition, non-capitalizable expenditures of $208 and $341 related to the Poinciana Parkway were expensed during the three months ended March 31, 2010 and 2009, respectively. At March 31, 2010, the carrying value of the Poinciana Parkway is $8,452.

Assuming that no additional significant adverse changes in our business occur, we anticipate, the aggregate cash on hand, cash flow generated through homebuilding and related operations, and sales of commercial and industrial and other land, will provide sufficient liquidity to fund our business for 2010.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

There have been no significant changes to our critical accounting policies and estimates during the three months ended March 31, 2010 as compared to those we disclosed in Management s Discussion and Analysis of Financial Condition and Results of Operations included in our 2009 Annual Report on Form 10-K.

RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

In June 2009, the FASB issued ASC 810, *Consolidation* (ASC 810). This guidance requires an enterprise to determine whether its variable interest or interests give it a controlling financial interest in a variable interest entity. The primary beneficiary of a variable interest entity is the enterprise that has both (1) the power to direct the activities of a variable interest entity that most significantly impact the entity s economic performance and (2) the obligation to absorb losses of the entity that could potentially be significant to the variable interest entity or the right to receive benefits from the entity that could potentially be significant to the variable interest entity. ASC 810 requires ongoing reassessments of whether an enterprise is the primary beneficiary of a variable interest entity. ASC 810 is effective for all variable interest entities and relationships with variable interest entities existing as of January 1, 2010. We adopted this standard on January 1, 2010, which did not have an impact on our consolidated financial position, results of operations or cash flows.

Item 3. Quantitative and Qualitative Disclosure About Market Risk

There have been no material changes in Avatar s market risk during the three months ended March 31, 2010. For additional information regarding Avatar s market risk, refer to Item 7A, Quantitative and Qualitative Disclosures About Market Risk, in our 2009 Annual Report on Form 10-K.

Item 4. Controls and Procedures

Under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, we evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934) as of the end of the period covered by this report. Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective for the purpose of ensuring that material information required to be in this report is made known to our management, including our Chief Executive Officer and Chief Financial Officer, and others, as appropriate, to allow timely decisions regarding required disclosures and are effective to provide reasonable assurance that such information is recorded, processed, summarized and reported within the time periods specified in the SEC s rules and forms.

Under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, we have determined that, during the fiscal quarter ended March 31, 2010, there were no changes in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934) that have affected, or are reasonably likely to affect, materially, our internal control over financial reporting.

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PART II OTHER INFORMATION

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds (dollars in thousands except share and per share data)

Repurchases of Equity Securities

For the three months ended March 31, 2010, Avatar repurchased shares as reflected in the following table:

Period	Total Number of Shares Purchased	Average Price Paid Per Share	Total Number of Shares Purchased as Part of a Publicly Announced Plan or Program (1)	Maximum Amount That May Yet Be Purchased Under the Plan or Program (1)
January 1, 2010 to January 31, 2010				$ 18,304
February 1, 2010 to February 28, 2010				$ 18,304
March 1, 2010 to March 31, 2010				$ 18,304
Total				

(1) On October 13, 2008, our Board of Directors amended its June 2005 authorization to purchase the 4.50% Notes and/or common stock to allow expenditures up to $30,000, including the $9,864 previously authorized. On October 17, 2008, we repurchased $35,920 principal amount of the 4.50% Notes for approximately $28,112

including accrued interest. On December 12, 2008, our Board of Directors amended its June 2005 authorization to purchase the 4.50% Notes and/or common stock to allow expenditures up to $30,000, including the $1,888 remaining after the October 2008 activities. On March 30, 2009, we repurchased $7,500 principal amount of the 4.50% Notes for approximately $6,038 including accrued interest. On June 19, 2009, we repurchased $6,576 principal amount of the 4.50% Notes for approximately $5,658 including accrued interest. As of March 31, 2010, the remaining authorization is $18,304.

Item 5. Other Information (dollars in thousands)

On May 3, 2010, we paid in full the outstanding principal and accrued interest of $55,979 under our Amended and Restated Credit Agreement. In addition, on May 4, 2010, we deposited $22,035 with Wells Fargo, N.A., successor by merger with Wachovia Bank, N.A., to secure the retirement of letters of credit outstanding under the credit facility. In connection with such payment and deposit, we notified our administrative agent that we were exercising our right to reduce our commitment amount under the facility to zero dollars ($0), which has the effect of terminating all parties obligations under the credit facility, effective no later than May 17, 2010. As of May 4, 2010, we had unrestricted cash and cash equivalents of approximately $161,000 and restricted cash of $22,035 deposited as security for the letters of credit.

On May 6, 2010, we entered into a First Amendment to Amended and Restated Employment Agreement (the First Amendment) with Randy Kotler, our Executive Vice President, Treasurer and Chief Financial Officer (Principal Financial Officer), which amends Mr. Kotler s employment agreement dated as of December 22, 2008 (the Employment Agreement) by, among other things, extending the term of his employment and modifying the compensation and termination provisions of the Employment Agreement. In particular, the First Amendment (1) extends the term of Mr. Kotler s employment from July 8, 2010 to December 31, 2010, (2) increases his annual base salary from $350 to $450 effective July 9, 2010, (3) eliminates the provision for payment of an annual bonus, (4) continues payment of an automobile allowance of $1 per month, and (5) provides that Mr. Kotler may terminate his employment by giving 90 days prior written notice of termination. Should Mr. Kotler be terminated Without Cause (as defined in the Employment Agreement filed as Exhibit 10.12 to Form 8-K filed with the Securities and Exchange Commission on December 30, 2008), he would continue to be compensated through December 31, 2010.

Item 6. Exhibits

10.1 First Amendment to Amended and Restated Employment Agreement, dated May 6, 2010, between Avatar Holdings Inc. and Randy Kotler (filed herewith)

31.1 Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).

31.2 Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).

32.1 Certification of Chief Executive Officer required by 18 U.S.C. Section 1350 (as adopted by Section 906 of the Sarbanes-Oxley Act of 2002) (furnished herewith).

32.2 Certification of Chief Financial Officer required by 18 U.S.C. Section 1350 (as adopted by Section 906 of the Sarbanes-Oxley Act of 2002) (furnished herewith).

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SIGNATURES

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

	AVATAR HOLDINGS INC.
Date: May 10, 2010	By: /s/ Randy L. Kotler Randy L. Kotler Executive Vice President, Chief Financial Officer and Treasurer (Principal Financial Officer)
Date: May 10, 2010	By: /s/ Michael P. Rama Michael P. Rama Controller and Chief Accounting Officer (Principal Accounting Officer)

Exhibit Index

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