

RYDER SYSTEM INC
Form 10-Q
October 24, 2007

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**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q**

b

**QUARTERLY REPORT
PURSUANT TO SECTION 13
OR 15(d)
OF THE SECURITIES
EXCHANGE ACT OF 1934
FOR THE QUARTERLY
PERIOD ENDED SEPTEMBER
30, 2007**

OR

o

**TRANSITION REPORT
PURSUANT TO SECTION 13
OR 15(d)
OF THE SECURITIES
EXCHANGE ACT OF 1934
FOR THE TRANSITION
PERIOD FROM _____ TO
_____**

**Commission File Number: 1-4364
RYDER SYSTEM, INC.**

(Exact name of registrant as specified in its charter)

Florida

(State or other jurisdiction of incorporation or organization)

59-0739250

(I.R.S. Employer Identification No.)

11690 N.W. 105th Street

Miami, Florida 33178

(Address of principal executive offices, including zip code)

(305) 500-3726

(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 NO

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer" and "large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer

Accelerated filer

Non-accelerated filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

YES NO

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The number of shares of Ryder System, Inc. Common Stock (\$0.50 par value per share) outstanding at September 30, 2007 was 58,027,630.

RYDER SYSTEM, INC.
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PART I. FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS
RYDER SYSTEM, INC. AND SUBSIDIARIES
CONSOLIDATED CONDENSED STATEMENTS OF EARNINGS
(unaudited)

	Three months ended September 30,		Nine months ended September 30,	
	2007	2006	2007	2006
	(In thousands, except per share amounts)			
Revenue	\$ 1,647,724	1,620,549	\$ 4,899,795	4,712,566
Operating expense (exclusive of items shown separately)	691,299	700,129	2,052,840	2,064,143
Salaries and employee-related costs	348,405	354,221	1,047,271	1,035,712
Subcontracted transportation	233,638	220,367	737,853	637,856
Depreciation expense	207,814	187,992	606,268	549,622
Gains on vehicle sales, net	(8,111)	(11,045)	(36,677)	(38,834)
Equipment rental	28,491	25,399	78,350	76,327
Interest expense	40,199	36,395	120,410	102,853
Miscellaneous income, net	(10,407)	(408)	(13,781)	(6,211)
Restructuring and other charges (recoveries), net	11,903	86	13,594	(73)
	1,543,231	1,513,136	4,606,128	4,421,395
Earnings before income taxes	104,493	107,413	293,667	291,171
Provision for income taxes	38,960	42,136	111,752	108,033
Net earnings	\$ 65,533	65,277	\$ 181,915	183,138
Earnings per common share:				
Basic	\$ 1.12	1.07	\$ 3.04	3.00
Diluted	\$ 1.11	1.06	\$ 3.01	2.97
Cash dividends per common share	\$ 0.21	0.18	\$ 0.63	0.54

See accompanying notes to consolidated condensed financial statements.

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RYDER SYSTEM, INC. AND SUBSIDIARIES
CONSOLIDATED CONDENSED BALANCE SHEETS

	(unaudited)	
	September	December
	30,	31,
	2007	2006
	(Dollars in thousands, except per share amount)	
Assets:		
Current assets:		
Cash and cash equivalents	\$ 106,231	128,639
Receivables, net	905,651	883,478
Inventories	58,077	59,318
Prepaid expenses and other current assets	202,066	190,381
Total current assets	1,272,025	1,261,816
Revenue earning equipment, net of accumulated depreciation of \$2,710,568 and \$2,825,876, respectively	4,537,190	4,509,332
Operating property and equipment, net of accumulated depreciation of \$803,945 and \$778,550, respectively	511,221	498,968
Goodwill	160,568	159,244
Intangible assets	13,789	14,387
Direct financing leases and other assets	390,834	385,176
Total assets	\$ 6,885,627	6,828,923
Liabilities and shareholders' equity:		
Current liabilities:		
Short-term debt and current portion of long-term debt	\$ 385,889	332,745
Accounts payable	438,483	515,121
Accrued expenses and other current liabilities	473,752	419,756
Total current liabilities	1,298,124	1,267,622
Long-term debt	2,430,206	2,484,198
Other non-current liabilities	402,253	449,158
Deferred income taxes	968,779	907,166
Total liabilities	5,099,362	5,108,144
Shareholders' equity:		
Preferred stock of no par value per share authorized, 3,800,917; none outstanding, September 30, 2007 or December 31, 2006		

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Common stock of \$0.50 par value per share authorized, 400,000,000; outstanding, September 30, 2007 58,027,630; December 31, 2006 60,721,528	28,854	30,220
Additional paid-in capital	724,508	713,264
Retained earnings	1,100,371	1,123,789
Accumulated other comprehensive loss	(67,468)	(146,494)
Total shareholders equity	1,786,265	1,720,779
Total liabilities and shareholders equity	\$ 6,885,627	6,828,923

See accompanying notes to consolidated condensed financial statements.

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RYDER SYSTEM, INC. AND SUBSIDIARIES
CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS
(unaudited)

	Nine months ended September 30,	
	2007	2006
	(In thousands)	
Cash flows from operating activities:		
Net earnings	\$ 181,915	183,138
Depreciation expense	606,268	549,622
Gains on vehicle sales, net	(36,677)	(38,834)
Share-based compensation expense	13,419	10,096
Amortization expense and other non-cash (credits) charges, net	(4,157)	11,778
Deferred income tax expense	53,554	69,141
Tax benefits from share-based compensation	1,450	4,643
Changes in operating assets and liabilities:		
Receivables	(2,788)	(95,301)
Inventories	1,824	(2,187)
Prepaid expenses and other assets	6,202	(48,334)
Accounts payable	24,958	79,603
Accrued expenses and other non-current liabilities	(8,642)	(111,761)
 Net cash provided by operating activities	 837,326	 611,604
 Cash flows from financing activities:		
Net change in commercial paper borrowings	(313,833)	265,164
Debt proceeds	697,234	338,307
Debt repaid, including capital lease obligations	(429,728)	(168,524)
Dividends on common stock	(37,967)	(33,080)
Common stock issued	40,798	53,977
Common stock repurchased	(209,018)	(141,531)
Excess tax benefits from share-based compensation	3,290	7,798
 Net cash (used in) provided by financing activities	 (249,224)	 322,111
 Cash flows from investing activities:		
Purchases of property and revenue earning equipment	(1,093,545)	(1,171,561)
Sales of revenue earning equipment	280,671	253,482
Sales of operating property and equipment	15,898	3,387
Sale and leaseback of revenue earning equipment	150,348	
Acquisitions		(4,113)
Collections on direct finance leases	46,992	51,287
Changes in restricted cash	(17,767)	(71,789)
Other, net	1,040	2,164
 Net cash used in investing activities	 (616,363)	 (937,143)

Effect of exchange rate changes on cash	5,853	2,792
Decrease in cash and cash equivalents	(22,408)	(636)
Cash and cash equivalents at January 1	128,639	128,727
Cash and cash equivalents at September 30	\$ 106,231	128,091
Supplemental disclosures of cash flow information:		
Cash paid during the period for:		
Interest	\$ 94,559	74,527
Income taxes, net of refunds	46,731	126,744
Non-cash investing activities:		
Changes in accounts payable related to purchases of revenue earning equipment	(111,465)	91,558
Revenue earning equipment acquired under capital leases	11,340	91
<i>See accompanying notes to consolidated condensed financial statements.</i>		

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RYDER SYSTEM, INC. AND SUBSIDIARIES
CONSOLIDATED CONDENSED STATEMENT OF SHAREHOLDERS EQUITY
(unaudited)

	Preferred Stock Amount	Common Stock Shares	Common Stock Par	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Total
	(Dollars in thousands, except per share amount)						
Balance at December 31, 2006	\$	60,721,528	\$ 30,220	713,264	1,123,789	(146,494)	1,720,779
Components of comprehensive income:							
Net earnings					181,915		181,915
Foreign currency translation adjustments						60,186	60,186
Unrealized loss related to derivative instruments						(37)	(37)
Amortization of transition obligation ⁽¹⁾						(17)	(17)
Amortization of net actuarial loss ⁽¹⁾						9,844	9,844
Amortization of prior service credit ⁽¹⁾						(1,460)	(1,460)
Pension curtailment ⁽²⁾						10,510	10,510
Total comprehensive income							260,941
Common stock dividends declared \$0.63 per share					(37,967)		(37,967)
Common stock issued under employee stock option and stock purchase plans ⁽³⁾		1,187,756	575	40,158			40,733
Benefit plan stock sales ⁽⁴⁾		844		65			65
Common stock repurchases		(3,882,498)	(1,941)	(47,138)	(159,939)		(209,018)
Share-based compensation				13,419			13,419
Tax benefits from share-based compensation				4,740			4,740
Adoption of FIN 48 ⁽⁵⁾					(7,427)		(7,427)
Balance at September 30, 2007	\$	58,027,630	\$ 28,854	724,508	1,100,371	(67,468)	1,786,265

(1) Amounts pertain to our pension and postretirement benefit plans and are

presented net of tax.

- (2) *See Note (M), Employee Benefit Plans, in the Notes to Consolidated Condensed Financial Statements for additional information related to the U.S. pension benefit plan curtailment.*
- (3) *Net of common shares delivered as payment for the exercise price or to satisfy the option holders withholding tax liability upon exercise of options.*
- (4) *Represents open-market transactions of common shares by the trustee of Ryder's deferred compensation plans.*
- (5) *See Note (B), Accounting Change, in the Notes to Consolidated Condensed Financial Statements for additional information related to the adoption of FIN 48, Accounting for Uncertainty in Income Taxes.*

See accompanying notes to consolidated condensed financial statements.

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RYDER SYSTEM, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS
(unaudited)

(A) INTERIM FINANCIAL STATEMENTS

The accompanying unaudited Consolidated Condensed Financial Statements include the accounts of Ryder System, Inc. (Ryder) and all entities in which Ryder System, Inc. has a controlling voting interest (subsidiaries), and variable interest entities (VIEs) required to be consolidated in accordance with U.S. generally accepted accounting principles (GAAP). The accompanying unaudited Consolidated Condensed Financial Statements have been prepared in accordance with the accounting policies described in the 2006 Annual Report on Form 10-K except for the accounting change described below relating to uncertain tax positions, and should be read in conjunction with the Consolidated Financial Statements and notes thereto. These statements do not include all of the information and footnotes required by GAAP in the United States of America for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included and the disclosures herein are adequate. The operating results for interim periods are unaudited and are not necessarily indicative of the results that can be expected for a full year. Certain prior year amounts have been reclassified to conform to the current period presentation.

(B) ACCOUNTING CHANGE

Prior to January 1, 2007, we recognized income tax accruals with respect to uncertain tax positions based upon Statement of Financial Accounting Standards (SFAS) No. 5, Accounting for Contingencies. Under SFAS No. 5, we recorded a liability associated with an uncertain tax position if the liability was both probable and estimable. Our liability under SFAS No. 5 included interest and penalties, which were recognized as incurred within Provision for income taxes in the Consolidated Condensed Statements of Earnings.

Effective January 1, 2007, we adopted Financial Accounting Standards Board (FASB) Interpretation No. (FIN) 48, Accounting for Uncertainty in Income Taxes. FIN 48 clarifies the accounting for uncertainty in income taxes recognized in financial statements in accordance with SFAS No. 109, Accounting for Income Taxes. FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 requires that we determine whether the benefits of our tax positions are more likely than not of being sustained upon audit based on the technical merits of the tax position. For tax positions that are more likely than not of being sustained upon audit, we recognize the largest amount of the benefit that is more likely than not of being sustained in our consolidated financial statements. For all other tax positions, we do not recognize any portion of the benefit in our consolidated financial statements. The provisions of FIN 48 also provide guidance on derecognition, classification, interest and penalties, accounting in interim periods and disclosure.

The cumulative effect of the adoption of the recognition and measurement provisions of FIN 48 resulted in a \$7.4 million reduction to the January 1, 2007 balance of retained earnings. Results of prior periods have not been restated. Our policy for interest and penalties related to income tax exposures was not impacted as a result of the adoption of the recognition and measurement provisions of FIN 48. Therefore, we continue to recognize interest and penalties as incurred within Provision for income taxes in the Consolidated Condensed Statements of Earnings. We expect the adoption of FIN 48 to increase our full-year 2007 effective tax rate by approximately 0.3%.

(C) SHARE-BASED COMPENSATION PLANS

Share-based incentive awards are provided to employees under the terms of various share-based compensation plans (collectively, the Plans). The Plans are administered by the Compensation Committee of the Board of Directors. Awards under the Plans principally include at-the-money stock options and nonvested stock (time-vested restricted stock rights, market-based restricted stock rights and restricted stock units). Share-based compensation expense is generally recorded in Salaries and employee-related costs in the Consolidated Condensed Statements of Earnings.

We grant restricted stock units (RSUs) to non-management members of the Board of Directors. Once granted, RSUs are eligible for dividends but have no voting rights. The fair value of the awards is determined and fixed on the grant date based on Ryder's stock price on the date of grant. The board member receives the RSUs upon their departure from the Board. The initial grant of RSUs will not vest unless the director has served a minimum of one year. When

the board member receives the RSUs, they are redeemed for an equivalent number of shares of Ryder's common stock. Compensation expense for RSUs was historically based on assumed years of service to retirement at age 72, as discussed in our 2007 Proxy Statement. However, because the RSUs do not contain an explicit service vesting period, except for the initial grant, compensation expense should have been recognized in the year

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RYDER SYSTEM, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS
(unaudited)

the RSUs were granted rather than over the assumed years of service. The one-time impact of accelerating the recognition of compensation expense on previously issued RSUs was a pre-tax charge of \$1.8 million recognized during the second quarter of 2007.

The following table provides information on share-based compensation expense and income tax benefits recognized during the periods:

	Three months ended September 30,		Nine months ended September 30,	
	2007	2006	2007	2006
	(In thousands)			
Stock option and stock purchase plans	\$ 2,515	2,784	\$ 7,490	7,776
Nonvested stock	1,393	924	5,929	2,320
Share-based compensation expense	3,908	3,708	13,419	10,096
Income tax benefit	(1,313)	(1,142)	(4,468)	(2,973)
Share-based compensation expense, net of tax (1)	\$ 2,595	2,566	\$ 8,951	7,123

(1) *In addition to the share-based compensation expense above, we recognized compensation expense of \$0.2 million and \$0.5 million during the three and nine months ended September 30, 2006, respectively, related to future cash awards issued in tandem with market-based restricted stock rights. Compensation expense for the cash awards was not*

significant in 2007.

Total unrecognized compensation expense related to share-based compensation arrangements at September 30, 2007 was \$22.7 million and is expected to be recognized over a weighted-average period of approximately 1.9 years.

During the nine months ended September 30, 2007 and 2006, 0.9 million and 1.1 million stock options, respectively, were granted under the Plans. These awards, which vest one-third each year, are fully vested three years from the grant date and have a contractual term of seven years. The fair value of each option award was estimated using a Black-Scholes-Merton option-pricing valuation model. The weighted-average grant-date fair value of options granted during the nine months ended September 30, 2007 and 2006 was \$12.82 and \$10.76, respectively.

During each of the nine months ended September 30, 2007 and 2006, 0.1 million awards of restricted stock rights and RSUs were granted under the Plans. The time-vested restricted stock rights entitle the holder to shares of common stock as the awards vest over a three-year period. The majority of the restricted stock rights granted during the period included a market-based vesting provision. Under such provision, the employees only receive the grant of stock if Ryder's total shareholder return (TSR) as a percentage of the S&P 500 comparable period TSR is 100% or greater over a three-year period. The fair value of the market-based restricted stock rights was estimated using a lattice-based option-pricing valuation model that incorporates a Monte-Carlo simulation. The weighted-average grant-date fair value of restricted stock rights and RSUs granted during the nine months ended September 30, 2007 and 2006 was \$33.44 and \$31.04, respectively.

(D) EARNINGS PER SHARE

Basic earnings per common share are computed by dividing net earnings by the weighted-average number of common shares outstanding. Nonvested stock granted to employees and directors are not included in the computation of basic earnings per common share until the shares vest. Diluted earnings per common share reflect the dilutive effect of potential common shares from securities such as stock options, time-vested restricted stock rights and RSUs. Diluted earnings per common share also reflect the dilutive effect of market-based restricted stock rights (contingently issuable shares) if the vesting conditions have been met as of the balance sheet date assuming the balance sheet date is the end of the contingency period. The dilutive effect of stock options and nonvested stock is computed using the treasury stock method, which assumes any proceeds that could be obtained upon the exercise of stock options and vesting of nonvested stock would be used to purchase common shares at the average market price for the period. The assumed proceeds include the purchase price the grantee pays, the windfall tax benefit that we receive upon assumed exercise and the unrecognized compensation expense at the end of each period. We calculate the assumed proceeds from excess tax benefits based on the deferred tax assets actually recorded without consideration of as if deferred tax assets calculated under the provision of SFAS No. 123R, Share-Based Payment.

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RYDER SYSTEM, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)
(unaudited)

A reconciliation of the number of shares used in computing basic and diluted earnings per common share follows:

Three months ended September
30, &nb