

Expedia, Inc.  
Form 10-Q  
April 27, 2012  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
**WASHINGTON, D.C. 20549**

**FORM 10-Q**

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

**For the quarterly period ended March 31, 2012**

**OR**

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

**For the transition period from            to**

**Commission File Number: 000-51447**

**EXPEDIA, INC.**

**(Exact name of registrant as specified in its charter)**

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**Delaware**  
(State or other jurisdiction of  
incorporation or organization)

**20-2705720**  
(I.R.S. Employer  
Identification No.)

**333 108<sup>th</sup> Avenue NE**

**Bellevue, WA 98004**

(Address of principal executive office) (Zip Code)

**(425) 679-7200**

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

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

Large accelerated filer ☒ Accelerated filer ☐

Non-accelerated filer ☐ (Do not check if a smaller reporting company) Smaller reporting company ☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☒

The number of shares outstanding of each of the registrant's classes of common stock as of April 13, 2012 was:

|                                                    |                    |
|----------------------------------------------------|--------------------|
| Common stock, \$0.0001 par value per share         | 114,283,330 shares |
| Class B common stock, \$0.0001 par value per share | 12,799,999 shares  |

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**Expedia, Inc.**

**Form 10-Q**

**For the Quarter Ended March 31, 2012**

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**Table of Contents****Part I. Item 1. Consolidated Financial Statements****EXPEDIA, INC.****CONSOLIDATED STATEMENTS OF OPERATIONS**

(In thousands, except for per share data)

(Unaudited)

|                                                                                                                      | <b>Three months ended<br/>March 31,</b> |                  |
|----------------------------------------------------------------------------------------------------------------------|-----------------------------------------|------------------|
|                                                                                                                      | <b>2012</b>                             | <b>2011</b>      |
| Revenue                                                                                                              | \$ 816,488                              | \$ 727,835       |
| Costs and expenses:                                                                                                  |                                         |                  |
| Cost of revenue (1)                                                                                                  | 200,098                                 | 175,610          |
| Selling and marketing (including \$51,361 and \$53,944 with a related party)(1)                                      | 377,072                                 | 350,908          |
| Technology and content (1)                                                                                           | 108,911                                 | 86,807           |
| General and administrative (1)                                                                                       | 78,578                                  | 71,160           |
| Amortization of intangible assets                                                                                    | 3,422                                   | 5,834            |
| Legal reserves, occupancy tax and other                                                                              | (276)                                   | 2,358            |
| Operating income                                                                                                     | 48,683                                  | 35,158           |
| Other income (expense):                                                                                              |                                         |                  |
| Interest income                                                                                                      | 5,743                                   | 3,335            |
| Interest expense                                                                                                     | (21,392)                                | (22,522)         |
| Other, net                                                                                                           | (6,207)                                 | (7,182)          |
| Total other expense, net                                                                                             | (21,856)                                | (26,369)         |
| Income from continuing operations before income taxes                                                                | 26,827                                  | 8,789            |
| Provision for income taxes                                                                                           | (5,240)                                 | (2,886)          |
| Income from continuing operations                                                                                    | 21,587                                  | 5,903            |
| Discontinued operations, net of taxes                                                                                | (23,889)                                | 46,306           |
| Net income (loss)                                                                                                    | (2,302)                                 | 52,209           |
| Net income attributable to noncontrolling interests                                                                  | (979)                                   | (170)            |
| <b>Net income (loss) attributable to Expedia, Inc.</b>                                                               | <b>\$ (3,281)</b>                       | <b>\$ 52,039</b> |
| <b>Amounts attributable to Expedia, Inc.:</b>                                                                        |                                         |                  |
| Income from continuing operations                                                                                    | \$ 20,608                               | \$ 5,826         |
| Discontinued operations, net of taxes                                                                                | (23,889)                                | 46,213           |
| Net income (loss)                                                                                                    | \$ (3,281)                              | \$ 52,039        |
| <b>Earnings per share from continuing operations attributable to Expedia, Inc. available to common stockholders:</b> |                                         |                  |
| Basic                                                                                                                | \$ 0.15                                 | \$ 0.04          |
| Diluted                                                                                                              | 0.15                                    | 0.04             |
| <b>Earnings (loss) per share attributable to Expedia, Inc. available to common stockholders:</b>                     |                                         |                  |

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|                                                     |           |         |
|-----------------------------------------------------|-----------|---------|
| Basic                                               | \$ (0.02) | \$ 0.38 |
| Diluted                                             | (0.02)    | 0.37    |
| <b>Shares used in computing earnings per share:</b> |           |         |
| Basic                                               | 133,202   | 136,930 |
| Diluted                                             | 139,306   | 139,084 |
| Dividends declared per common share                 | \$ 0.09   | \$ 0.14 |

(1) Includes stock-based compensation as follows:

|                            |        |        |
|----------------------------|--------|--------|
| Cost of revenue            | \$ 919 | \$ 810 |
| Selling and marketing      | 4,445  | 3,509  |
| Technology and content     | 4,284  | 3,863  |
| General and administrative | 7,303  | 6,616  |

*See accompanying notes.*

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**EXPEDIA, INC.**

**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**

(In thousands)

(Unaudited)

|                                                                          | <b>Three months ended<br/>March 31,</b> |             |
|--------------------------------------------------------------------------|-----------------------------------------|-------------|
|                                                                          | <b>2012</b>                             | <b>2011</b> |
| Net income (loss)                                                        | \$ (2,302)                              | \$ 52,209   |
| Other comprehensive income, net of tax                                   |                                         |             |
| Currency translation adjustments                                         | 12,951                                  | 25,080      |
| Unrealized gains (losses) on available for sale securities, net of taxes | 1,402                                   | (34)        |
| Other comprehensive income                                               | 14,353                                  | 25,046      |
| Comprehensive income                                                     | 12,051                                  | 77,255      |
| Less: Comprehensive income attributable to noncontrolling interests      | (990)                                   | (775)       |
| Comprehensive income attributable to Expedia, Inc.                       | \$ 11,061                               | \$ 76,480   |

*See accompanying notes.*

**Table of Contents****EXPEDIA, INC.****CONSOLIDATED BALANCE SHEETS**

(In thousands, except per share data)

|                                                              | <b>March 31,<br/>2012<br/>(Unaudited)</b> | <b>December 31,<br/>2011</b> |
|--------------------------------------------------------------|-------------------------------------------|------------------------------|
| <b>ASSETS</b>                                                |                                           |                              |
| Current assets:                                              |                                           |                              |
| Cash and cash equivalents                                    | \$ 1,272,508                              | \$ 689,134                   |
| Restricted cash and cash equivalents                         | 23,274                                    | 19,082                       |
| Short-term investments                                       | 725,179                                   | 648,819                      |
| Accounts receivable, net of allowance of \$9,050 and \$7,959 | 414,555                                   | 339,427                      |
| Prepaid expenses and other current assets                    | 134,796                                   | 121,541                      |
| Current assets of discontinued operations                    | 14,330                                    | 456,426                      |
| Total current assets                                         | 2,584,642                                 | 2,274,429                    |
| Property and equipment, net                                  | 343,540                                   | 320,282                      |
| Long-term investments and other assets                       | 262,213                                   | 289,348                      |
| Intangible assets, net                                       | 738,858                                   | 743,898                      |
| Goodwill                                                     | 2,888,930                                 | 2,877,301                    |
| <b>TOTAL ASSETS</b>                                          | <b>\$ 6,818,183</b>                       | <b>\$ 6,505,258</b>          |
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>                  |                                           |                              |
| Current liabilities:                                         |                                           |                              |
| Accounts payable, merchant                                   | \$ 843,376                                | \$ 777,602                   |
| Accounts payable, other                                      | 200,872                                   | 173,855                      |
| Deferred merchant bookings                                   | 1,636,076                                 | 833,625                      |
| Deferred revenue                                             | 16,913                                    | 15,238                       |
| Accrued expenses and other current liabilities               | 304,952                                   | 333,237                      |
| Current liabilities of discontinued operations               |                                           | 419,800                      |
| Total current liabilities                                    | 3,002,189                                 | 2,553,357                    |
| Long-term debt                                               | 1,249,296                                 | 1,249,281                    |
| Deferred income taxes, net                                   | 287,925                                   | 279,962                      |
| Other long-term liabilities                                  | 123,274                                   | 117,491                      |
| Commitments and contingencies                                |                                           |                              |
| Stockholders' equity:                                        |                                           |                              |
| Common stock \$.0001 par value                               | 18                                        | 18                           |
| Authorized shares: 1,600,000                                 |                                           |                              |
| Shares issued: 178,777 and 176,378                           |                                           |                              |
| Shares outstanding: 117,240 and 120,781                      |                                           |                              |
| Class B common stock \$.0001 par value                       | 1                                         | 1                            |
| Authorized shares: 400,000                                   |                                           |                              |
| Shares issued and outstanding: 12,800 and 12,800             |                                           |                              |
| Additional paid-in capital                                   | 5,510,732                                 | 5,474,653                    |
| Treasury stock - Common stock, at cost                       | (2,733,383)                               | (2,535,219)                  |
| Shares: 61,537 and 55,597                                    |                                           |                              |
| Retained earnings (deficit)                                  | (725,520)                                 | (722,239)                    |
| Accumulated other comprehensive loss                         | (3,008)                                   | (17,350)                     |

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|                                                   |                     |                     |
|---------------------------------------------------|---------------------|---------------------|
| Total Expedia, Inc. stockholders' equity          | 2,048,840           | 2,199,864           |
| Noncontrolling interest                           | 106,659             | 105,303             |
| Total stockholders' equity                        | 2,155,499           | 2,305,167           |
| <b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b> | <b>\$ 6,818,183</b> | <b>\$ 6,505,258</b> |

*See accompanying notes.*

**Table of Contents****EXPEDIA, INC.****CONSOLIDATED STATEMENTS OF CASH FLOWS**

(In thousands)

(Unaudited)

|                                                                                                              | <b>Three months ended March 31,</b> |                  |
|--------------------------------------------------------------------------------------------------------------|-------------------------------------|------------------|
|                                                                                                              | <b>2012</b>                         | <b>2011</b>      |
| <b>Operating activities:</b>                                                                                 |                                     |                  |
| Net income (loss)                                                                                            | \$ (2,302)                          | \$ 52,209        |
| Less: Discontinued operations, net of tax                                                                    | (23,889)                            | 46,306           |
| Net income from continuing operations                                                                        | 21,587                              | 5,903            |
| Adjustments to reconcile net income from continuing operations to net cash provided by operating activities: |                                     |                  |
| Depreciation of property and equipment, including internal-use software and website development              | 34,314                              | 29,185           |
| Amortization of stock-based compensation                                                                     | 16,951                              | 14,798           |
| Amortization of intangible assets                                                                            | 3,422                               | 5,834            |
| Deferred income taxes                                                                                        | 10,323                              | 379              |
| Foreign exchange gain on cash, cash equivalents and short-term investments, net                              | (12,021)                            | (4,371)          |
| Realized gain on foreign currency forwards                                                                   | (6,637)                             | (844)            |
| Other                                                                                                        | 3,921                               | (7,391)          |
| Changes in operating assets and liabilities, net of effects from acquisitions:                               |                                     |                  |
| Accounts receivable                                                                                          | (71,836)                            | (81,995)         |
| Prepaid expenses and other current assets                                                                    | (18,389)                            | (22,909)         |
| Accounts payable, merchant                                                                                   | 64,299                              | 100,605          |
| Accounts payable, other, accrued expenses and other current liabilities                                      | (2,248)                             | (26,054)         |
| Deferred merchant bookings                                                                                   | 802,457                             | 677,597          |
| Deferred revenue                                                                                             | 1,673                               | 1,914            |
| <b>Net cash provided by operating activities from continuing operations</b>                                  | <b>847,816</b>                      | <b>692,651</b>   |
| <b>Investing activities:</b>                                                                                 |                                     |                  |
| Capital expenditures, including internal-use software and website development                                | (50,814)                            | (46,086)         |
| Purchases of investments                                                                                     | (293,190)                           | (676,568)        |
| Sales and maturities of investments                                                                          | 240,641                             | 297,295          |
| Net settlement of foreign currency forwards                                                                  | 6,637                               | 844              |
| Other, net                                                                                                   | (1,031)                             | 430              |
| <b>Net cash used in investing activities from continuing operations</b>                                      | <b>(97,757)</b>                     | <b>(424,085)</b> |
| <b>Financing activities:</b>                                                                                 |                                     |                  |
| Treasury stock activity                                                                                      | (198,164)                           | (47,928)         |
| Payment of dividends to stockholders                                                                         | (12,204)                            | (19,352)         |
| Proceeds from exercise of equity awards                                                                      | 31,801                              | 3,285            |
| Excess tax benefit on equity awards                                                                          | 7,492                               | 1,087            |
| Changes in restricted cash and cash equivalents                                                              | (4,197)                             | (5,716)          |
| Other, net                                                                                                   | 21                                  | 1,141            |
| <b>Net cash used in financing activities from continuing operations</b>                                      | <b>(175,251)</b>                    | <b>(67,483)</b>  |
| <b>Net cash provided by continuing operations</b>                                                            | <b>574,808</b>                      | <b>201,083</b>   |
| <b>Net cash provided by (used in) discontinued operations</b>                                                | <b>(7,607)</b>                      | <b>40,202</b>    |

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|                                                               |                     |                   |
|---------------------------------------------------------------|---------------------|-------------------|
| Effect of exchange rate changes on cash and cash equivalents  | 16,173              | 8,769             |
| <b>Net increase in cash and cash equivalents</b>              | <b>583,374</b>      | <b>250,054</b>    |
| Cash and cash equivalents at beginning of period              | 689,134             | 621,199           |
| <b>Cash and cash equivalents at end of period</b>             | <b>\$ 1,272,508</b> | <b>\$ 871,253</b> |
| <b>Supplemental cash flow information</b>                     |                     |                   |
| Cash paid for interest from continuing operations             | \$ 42,667           | \$ 43,391         |
| Income tax payments (refunds), net from continuing operations | (17,231)            | 3,109             |
| <i>See accompanying notes.</i>                                |                     |                   |

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### **Notes to Consolidated Financial Statements**

**March 31, 2012**

**(Unaudited)**

#### **Note 1 Basis of Presentation**

##### ***Description of Business***

Expedia, Inc. and its subsidiaries provide travel products and services to leisure and corporate travelers in the United States and abroad as well as various media and advertising offerings to travel and non-travel advertisers. These travel products and services are offered through a diversified portfolio of brands including: Expedia.com®, Hotels.com®, Hotwire.com, Expedia® Affiliate Network, Classic Vacations, Expedia Local Expert, Egencia, Expedia® CruiseShipCenters®, eLong, Inc. (eLong) and Venere Net SpA (Venere). In addition, many of these brands have related international points of sale. We refer to Expedia, Inc. and its subsidiaries collectively as Expedia, the Company, us, we and our these consolidated financial statements.

##### ***TripAdvisor Spin-Off***

On December 20, 2011, following the close of trading on the Nasdaq Stock Market, we completed the spin-off of TripAdvisor, Inc. (TripAdvisor), which consisted of the domestic and international operations previously associated with our TripAdvisor Media Group, to Expedia stockholders. We refer to this transaction as the spin-off. Immediately prior to the spin-off, Expedia effected a one-for-two reverse stock split. Accordingly, the results of operations, financial condition and cash flows of TripAdvisor have been presented as discontinued operations for all periods presented. Further, all Expedia common stock share information and related per share amounts in prior periods have been adjusted to reflect Expedia's one-for-two reverse stock split.

##### ***Basis of Presentation***

These accompanying financial statements present our results of operations, financial position and cash flows on a consolidated basis. The unaudited consolidated financial statements include Expedia, Inc., our wholly-owned subsidiaries, and entities we control, or in which we have a variable interest and are the primary beneficiary of expected cash profits or losses. We have eliminated significant intercompany transactions and accounts.

We have prepared the accompanying unaudited consolidated financial statements in accordance with accounting principles generally accepted in the United States (GAAP) for interim financial reporting. We have included all adjustments necessary for a fair presentation of the results of the interim period. These adjustments consist of normal recurring items. Our interim unaudited consolidated financial statements are not necessarily indicative of results that may be expected for any other interim period or for the full year. These interim unaudited consolidated financial statements should be read in conjunction with the audited consolidated financial statements and related notes included in our Annual Report on Form 10-K for the year ended December 31, 2011, previously filed with the Securities and Exchange Commission.

##### ***Accounting Estimates***

We use estimates and assumptions in the preparation of our interim unaudited consolidated financial statements in accordance with GAAP. Our estimates and assumptions affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of our interim unaudited consolidated financial statements. These estimates and assumptions also affect the reported amount of net income during any period. Our actual financial results could differ significantly from these estimates. The significant estimates underlying our interim unaudited consolidated financial statements include revenue recognition; recoverability of current and long-lived assets, intangible assets and goodwill; income and indirect taxes, such as potential settlements related to occupancy taxes; loss contingencies; loyalty program liabilities; stock-based compensation and accounting for derivative instruments.

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**Notes to Consolidated Financial Statements - (Continued)**

***Reclassifications***

We have reclassified certain amounts related to our prior period results to conform to our current period presentation.

***Seasonality***

We generally experience seasonal fluctuations in the demand for our travel products and services. For example, traditional leisure travel bookings are generally the highest in the first three quarters as travelers plan and book their spring, summer and holiday travel. The number of bookings typically decreases in the fourth quarter. Because revenue in our merchant business is generally recognized when the travel takes place rather than when it is booked, revenue typically lags bookings by several weeks or longer. The seasonal revenue impact is exacerbated with respect to income by the more stable nature of our fixed costs. As a result, revenue and income are typically the lowest in the first quarter and highest in the third quarter. In addition, as a result of the spin-off, the seasonal fluctuation on our revenue and operating income will be more pronounced, particularly in the first quarter.

**Note 2 Summary of Significant Accounting Policies**

***Recently Adopted Accounting Pronouncements***

On January 1, 2012, we adopted the new Financial Accounting Standards Board guidance on the presentation of comprehensive income. Specifically, the new guidance allows an entity to present components of net income and other comprehensive income in one continuous statement, referred to as the statement of comprehensive income, or in two separate, but consecutive statements, which is the approach we have selected. The new guidance eliminated the option to report other comprehensive income and its components in the statement of changes in stockholders' equity. While the new guidance changed the presentation of comprehensive income, there were no changes to the components that are recognized in net income or other comprehensive income from that of previous accounting guidance.

**NOTE 3 Acquisitions and Dispositions**

***Business Acquisitions.*** In March 2012, Egencia entered into an agreement to acquire VIA Travel, a travel management company in the Nordics. The transaction is expected to close in the second quarter of 2012.

***Discontinued Operations.*** On December 20, 2011, we completed the spin-off of TripAdvisor, Inc., which included its flagship brand as well as 18 other travel media brands. Accordingly, we have presented the financial condition and results of operations of our former TripAdvisor Media Group segment in the consolidated financial statements through December 20, 2011 as discontinued operations. Additionally, the first quarter 2012 loss incurred to extinguish our 8.5% senior notes due 2016 (the "8.5% Notes") as a result of the spin-off was recorded as discontinued operations. See below for a full description of the extinguishment. Financial data for the discontinued operations for the three months ended

**Table of Contents****Notes to Consolidated Financial Statements - (Continued)**

March 31, 2012 and 2011 were as follows:

|                                                                  | <b>Three months ended March 31,</b> |                  |
|------------------------------------------------------------------|-------------------------------------|------------------|
|                                                                  | <b>2012</b>                         | <b>2011</b>      |
|                                                                  | <b>(In thousands)</b>               |                  |
| Revenue                                                          | \$                                  | \$ 148,286       |
| Income (loss) before income taxes                                | (37,568)                            | 65,396           |
| Provision for income taxes                                       | 13,679                              | (19,090)         |
| Net income (loss)                                                | (23,889)                            | 46,306           |
| Net income attributable to noncontrolling interest               |                                     | (93)             |
| <b>Net income (loss) attributable to discontinued operations</b> | <b>\$ (23,889)</b>                  | <b>\$ 46,213</b> |
| <b>Earnings (loss) per share:</b>                                |                                     |                  |
| Basic                                                            | \$ (0.18)                           | \$ 0.34          |
| Diluted                                                          | (0.17)                              | 0.33             |
| <b>Shares used in computing earnings per share:</b>              |                                     |                  |
| Basic                                                            | 133,202                             | 136,930          |
| Diluted                                                          | 139,306                             | 139,084          |

The indenture governing our \$400 million aggregate principal amount of 8.5% Notes contained certain covenants that could have restricted implementation of the spin-off. On December 20, 2011, prior to consummation of the spin-off, we gave Notice of Redemption to the bondholders, the effect of which was the bonds became due and payable on the redemption date at the redemption price. The redemption price was equal to 100% of the principal amount plus a make-whole premium as of, and accrued and unpaid interest to, the redemption date. The redemption date was defined as 30 days after the Notice of Redemption was given. In order to complete the Notice of Redemption, we were required to irrevocably deposit, with the Trustee, funds sufficient to pay the redemption price plus accrued interest on the 8.5% Notes (approximately \$451 million). The 8.5% Notes were fully redeemed on January 19, 2012, the redemption date, for approximately \$450 million. In connection with the redemption, we incurred a pre-tax loss from early extinguishment of debt of approximately \$38 million (or \$24 million net of tax), which included an early redemption premium of \$33 million and the write-off of \$5 million of unamortized debt issuance and discount costs. This loss was recorded within discontinued operations in the first quarter of 2012, as that was the period in which the bonds were legally extinguished.

As a result of the above, at December 31, 2011, we had a current asset of discontinued operations of \$456 million primarily related to the deposit for the redemption price of the 8.5% Notes as well as a current liability of discontinued operations of \$420 million for the 8.5% Notes, accrued interest expense related to the 8.5% Notes and accrued spin-off costs. At March 31, 2012, the current asset of discontinued operations included a \$14 million tax benefit primarily related to the loss on the extinguishment of debt.

**Table of Contents****Notes to Consolidated Financial Statements - (Continued)****Note 4 Fair Value Measurements**

Financial assets and liabilities measured at fair value on a recurring basis as of March 31, 2012 are classified using the fair value hierarchy in the table below:

|                                    | <b>Total</b>     | <b>Level 1<br/>(In thousands)</b> | <b>Level 2</b> |
|------------------------------------|------------------|-----------------------------------|----------------|
| <b>Assets</b>                      |                  |                                   |                |
| Cash equivalents:                  |                  |                                   |                |
| Money market funds                 | \$ 754,146       | \$ 754,146                        | \$             |
| Time deposits                      | 18,109           |                                   | 18,109         |
| Investments:                       |                  |                                   |                |
| Time deposits                      | 650,683          |                                   | 650,683        |
| Corporate debt securities          | 260,812          |                                   | 260,812        |
| <br>Total assets                   | <br>\$ 1,683,750 | <br>\$ 754,146                    | <br>\$ 929,604 |
| <b>Liabilities</b>                 |                  |                                   |                |
| Foreign currency forward contracts | \$ 1,215         | \$                                | \$ 1,215       |

Financial assets measured at fair value on a recurring basis as of December 31, 2011 are classified using the fair value hierarchy in the table below:

|                                    | <b>Total</b>     | <b>Level 1<br/>(In thousands)</b> | <b>Level 2</b> |
|------------------------------------|------------------|-----------------------------------|----------------|
| <b>Assets</b>                      |                  |                                   |                |
| Cash equivalents:                  |                  |                                   |                |
| Money market funds                 | \$ 310,075       | \$ 310,075                        | \$             |
| Derivatives:                       |                  |                                   |                |
| Foreign currency forward contracts | 1,043            |                                   | 1,043          |
| Investments:                       |                  |                                   |                |
| Time deposits                      | 592,162          |                                   | 592,162        |
| Corporate debt securities          | 268,664          |                                   | 268,664        |
| <br>Total assets                   | <br>\$ 1,171,944 | <br>\$ 310,075                    | <br>\$ 861,869 |

We classify our cash equivalents and investments within Level 1 and Level 2 as we value our cash equivalents and investments using quoted market prices or alternative pricing sources and models utilizing market observable inputs. Valuation of the foreign currency forward contracts is based on foreign currency exchange rates in active markets, a Level 2 input.

As of March 31, 2012 and December 31, 2011, our cash and cash equivalents consisted primarily of prime institutional money market funds with maturities of 90 days or less, time deposits as well as bank account balances.

We invest in investment grade corporate debt securities all of which are classified as available for sale. As of March 31, 2012, we had \$75 million of short-term and \$186 million of long-term available for sale investments and the amortized cost basis of the investments approximated their fair value with gross unrealized gains of \$3 million and gross unrealized losses of less than \$1 million. As of December 31, 2011, we had \$57 million of short-term and \$212 million of long-term available for sale investments and the amortized cost basis of these investments

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approximated their fair value with gross unrealized gains of \$2 million and gross unrealized losses of \$1 million.

We also hold time deposit investments with financial institutions. Time deposits with original maturities of less than 90 days are classified as cash equivalents and those with remaining maturities of less than one year are classified as short-term investments. Of the total time deposit investments, \$250 million and \$228 million as of March 31, 2012 and December 31, 2011 related to balances held by our majority-owned subsidiaries.

**Table of Contents****Notes to Consolidated Financial Statements - (Continued)**

Derivative instruments are carried at fair value on our consolidated balance sheets. We use foreign currency forward contracts to economically hedge certain merchant revenue exposures and in lieu of holding certain foreign currency cash for the purpose of economically hedging our foreign currency-denominated operating liabilities. Our goal in managing our foreign exchange risk is to reduce, to the extent practicable, our potential exposure to the changes that exchange rates might have on our earnings, cash flows and financial position. Our foreign currency forward contracts are typically short-term and, as they do not qualify for hedge accounting treatment, we classify the changes in their fair value in other, net. As of March 31, 2012, we were party to outstanding forward contracts hedging our liability and revenue exposures with a total net notional value of \$128 million. We had a net forward liability of \$1 million as of March 31, 2012 recorded in accrued expenses and other current liabilities and a net forward asset of \$1 million as of December 31, 2011 recorded in prepaid expenses and other current assets. We recorded \$1 million in net gains and \$2 million in net losses from foreign currency forward contracts during the three months ended March 31, 2012 and 2011.

**Note 5 Debt**

The following table sets forth our outstanding debt:

|                                              | March 31,<br>2012 | December 31,<br>2011 |
|----------------------------------------------|-------------------|----------------------|
|                                              | (In thousands)    |                      |
| 7.456% senior notes due 2018                 | \$ 500,000        | \$ 500,000           |
| 5.95% senior notes due 2020, net of discount | 749,296           | 749,281              |
| Long-term debt                               | \$ 1,249,296      | \$ 1,249,281         |

We have excluded from the above table the \$400 million 8.5% Notes, which were included in current liabilities of discontinued operations as of December 31, 2011 in the consolidated balance sheets, which were redeemed on January 19, 2012. For further information, see Note 3 Acquisitions and Dispositions.

**Long-term Debt**

Our \$500 million in registered senior unsecured notes outstanding at March 31, 2012 are due in August 2018 and bear interest at 7.456% (the 7.456% Notes). Interest is payable semi-annually in February and August of each year. The 7.456% Notes are repayable in whole or in part on August 15, 2013, at the option of the holders of such 7.456% Notes, at 100% of the principal amount plus accrued interest. We may redeem the 7.456% Notes at a redemption price of 100% of the principal plus accrued interest, plus a make-whole premium, in whole or in part at any time at our option.

Our \$750 million in registered senior unsecured notes outstanding at March 31, 2012 are due in August 2020 and bear interest at 5.95% (the 5.95% Notes). The 5.95% Notes were issued at 99.893% of par resulting in a discount, which is being amortized over their life. Interest is payable semi-annually in February and August of each year. We may redeem the 5.95% Notes at a redemption price of 100% of the principal plus accrued interest, plus a make-whole premium, in whole or in part at any time or from time to time at our option.

The 7.456% and 5.95% Notes (collectively the Notes) are senior unsecured obligations guaranteed by certain domestic Expedia subsidiaries and rank equally in right of payment with all of our existing and future unsecured and unsubordinated obligations. For further information, see Note 12 Guarantor and Non-Guarantor Supplemental Financial Information. In addition, the Notes include covenants that limit our ability (i) to create or incur liens, (ii) to enter into sale/leaseback transactions and (iii) to merge or consolidate with or into another entity. Accrued interest related to the Notes was \$10 million and \$31 million as of March 31, 2012 and December 31, 2011.

Based on quoted market prices, the approximate fair value of 7.456% Notes was approximately \$566 million and \$563 million as of March 31, 2012, and December 31, 2011, and the approximate fair value of 5.95% Notes was approximately \$773 million and \$760 million as of March 31, 2012, and December 31, 2011.



**Table of Contents****Notes to Consolidated Financial Statements - (Continued)*****Credit Facility***

Expedia, Inc. maintains a \$750 million unsecured revolving credit facility with a group of lenders, which is unconditionally guaranteed by certain domestic Expedia subsidiaries that are the same as under the Notes and expires in August 2016. As of March 31, 2012 and December 31, 2011, we had no revolving credit facility borrowings outstanding. The facility bears interest based on the Company's credit ratings, with drawn amounts bearing interest at LIBOR plus 150 basis points and the commitment fee on undrawn amounts at 22.5 basis points as of March 31, 2012. The facility contains financial covenants including leverage and minimum interest coverage ratios.

The amount of stand-by letters of credit ( LOC ) issued under the facility reduces the credit amount available. As of March 31, 2012, and December 31, 2011, there was \$22 million of outstanding stand-by LOCs issued under the facility.

**Note 6 Stockholders' Equity*****Dividends on our Common Stock***

The Executive Committee, acting on behalf of the Board of Directors, declared the following dividends during the periods presented, which have been adjusted for the one-for-two reverse stock split in December 2011:

| Dividend         |           |                |                                |                |
|------------------|-----------|----------------|--------------------------------|----------------|
| Declaration Date | Per Share | Record Date    | Total Amount<br>(in thousands) | Payment Date   |
| February 9, 2012 | \$ 0.09   | March 12, 2012 | \$ 12,204                      | March 30, 2012 |
| February 9, 2011 | \$ 0.14   | March 11, 2011 | \$ 19,352                      | March 31, 2011 |

In addition, on April 25, 2012, the Executive Committee, acting on behalf of the Board of Directors, declared a quarterly cash dividend of \$0.09 per share of outstanding common stock to stockholders of record as of the close of business on May 30, 2012. Future declarations of dividends are subject to final determination of our Board of Directors.

***Share Repurchases***

In 2010, the Executive Committee, acting on behalf of the Board of Directors, authorized a repurchase of up to 20 million outstanding shares of our common stock. During the three months ended March 31, 2012, we repurchased, through open market transactions, 5.8 million shares under this authorization for a total cost of \$192 million, excluding transaction costs, representing an average repurchase price of \$33.39 per share. Subsequent to the end of the first quarter of 2012, we repurchased the additional 3 million shares remaining under the 2010 authorization for a total cost of \$99 million, excluding transaction costs, representing an average repurchase price of \$32.95 per share.

On April 25, 2012, the Executive Committee, acting on behalf of the Board of Directors, authorized a repurchase of up to 20 million outstanding shares of our common stock. No shares have been repurchased under this authorization and the authorization has no fixed termination date for the repurchases.

***Stock-based Awards***

Stock-based compensation expense relates primarily to expense for stock options and restricted stock units ( RSUs ). Our stock options generally vest over four years and our RSUs generally vest over five years.

As of March 31, 2012, we had stock-based awards outstanding representing approximately 20 million shares of our common stock consisting of options to purchase approximately 18 million shares of our common stock with a weighted average exercise price of \$22.46 and weighted average remaining life of 5.3 years and approximately 2 million RSUs.

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Annual employee stock-based award grants typically occur during the first quarter of each year. During the three months ended March 31, 2012, we granted approximately 5 million stock options.

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### Notes to Consolidated Financial Statements - (Continued)

The fair value of the stock options granted during the three months ended March 31, 2012 was estimated at the date of grant using the Black-Scholes option-pricing model with the following weighted average assumptions:

|                                                          |          |
|----------------------------------------------------------|----------|
| Risk-free interest rate                                  | 0.62%    |
| Expected volatility                                      | 53.12%   |
| Expected life (in years)                                 | 4        |
| Dividend yield                                           | 1.06%    |
| Weighted-average estimated fair value of options granted | \$ 12.94 |

As of March 31, 2012, there were 30 million privately held warrants outstanding, which if exercised in full, would entitle the holders to acquire 7.4 million common shares of Expedia, Inc. at a weighted average exercise price of \$24.16. All of these warrants expire in May 2012.

### Note 7 Earnings Per Share

The following table presents our basic and diluted earnings per share:

|                                                                                                                      | Three months ended March 31,        |                 |
|----------------------------------------------------------------------------------------------------------------------|-------------------------------------|-----------------|
|                                                                                                                      | 2012                                | 2011            |
|                                                                                                                      | In thousands, except per share data |                 |
| <b>Income from continuing operations attributable to Expedia, Inc.</b>                                               | <b>\$ 20,608</b>                    | <b>\$ 5,826</b> |
| <b>Earnings per share from continuing operations attributable to Expedia, Inc. available to common stockholders:</b> |                                     |                 |
| Basic                                                                                                                | \$ 0.15                             | \$ 0.04         |
| Diluted                                                                                                              | 0.15                                | 0.04            |
| <b>Weighted average number of shares outstanding:</b>                                                                |                                     |                 |
| Basic                                                                                                                | 133,202                             | 136,930         |
| Dilutive effect of:                                                                                                  |                                     |                 |
| Options to purchase common stock                                                                                     | 3,443                               | 1,635           |
| Other dilutive securities                                                                                            | 2,661                               | 519             |
| Diluted                                                                                                              | 139,306                             | 139,084         |

The earnings per share amounts are the same for common stock and Class B common stock because the holders of each class are legally entitled to equal per share distributions whether through dividends or in liquidation.

### Note 8 Income Taxes

We determine our provision for income taxes for interim periods using an estimate of our annual effective rate. We record any changes to the estimated annual rate in the interim period in which the change occurs, including discrete tax items. Our effective tax rate was 19.5% and 32.8% for the three months ended March 31, 2012 and 2011. The decrease in the effective rate for the three months ended March 31, 2012 as compared to the same period in 2011 was primarily due to a release of accruals related to uncertain tax positions and to a lesser extent an increase in estimated earnings in jurisdictions outside of the United States.

**Table of Contents****Notes to Consolidated Financial Statements - (Continued)****Note 9 Commitments and Contingencies*****Legal Proceedings***

In the ordinary course of business, we are a party to various lawsuits. Management does not expect these lawsuits to have a material impact on the liquidity, results of operations, or financial condition of Expedia. We also evaluate other potential contingent matters, including value-added tax, federal excise tax, transient occupancy or accommodation tax and similar matters. We do not believe that the aggregate amount of liability that could be reasonably possible with respect to these matters would have a material adverse effect on our financial results; however, litigation is inherently uncertain and the actual losses incurred in the event that our legal proceedings were to result in unfavorable outcomes could have a material adverse effect on our business and financial performance.

*Litigation Relating to Hotel Occupancy Taxes.* Seventy-nine lawsuits have been filed by cities, counties and states involving hotel occupancy taxes. Forty-nine lawsuits are currently active. These lawsuits are in various stages and we continue to defend against the claims made in them vigorously. With respect to the principal claims in these matters, we believe that the ordinances at issue do not apply to the services we provide, namely the facilitation of hotel reservations, and, therefore, that we do not owe the taxes that are claimed to be owed. We believe that the ordinances at issue generally impose occupancy and other taxes on entities that own, operate or control hotels (or similar businesses) or furnish or provide hotel rooms or similar accommodations. To date, twenty-eight of these lawsuits have been dismissed. Some of these dismissals have been without prejudice and, generally, allow the governmental entity or entities to seek administrative remedies prior to pursuing further litigation. Sixteen dismissals were based on a finding that we and the other defendants were not subject to the local hotel occupancy tax ordinance or that the local government lacked standing to pursue their claims. As a result of this litigation and other attempts by certain jurisdictions to levy such taxes, we have established a reserve for the potential settlement of issues related to hotel occupancy taxes, consistent with applicable accounting principles and in light of all current facts and circumstances, in the amount of \$31 million as of March 31, 2012 and \$32 million as of December 31, 2011. This reserve is based on our best estimate and the ultimate resolution of these contingencies may be greater or less than the liabilities recorded. In addition, as of March 31, 2012 and December 31, 2011, we had an accrual totaling \$1 million and \$10 million related to court decisions and final settlements. Changes to these settlement reserves are included within legal reserves, occupancy tax and other in the consolidated statements of operations.

In connection with various occupancy tax audits and assessments, certain jurisdictions may assert that taxpayers are required to pay any assessed taxes prior to being allowed to contest or litigate the applicability of the ordinances, which is referred to as pay-to-play. These jurisdictions may attempt to require that we pay any assessed taxes prior to being allowed to contest or litigate the applicability of the tax ordinance. Payment of these amounts is not an admission that we believe we are subject to such taxes and, even when such payments are made, we continue to defend our position vigorously. During 2010 and 2009, we expensed \$3 million and \$48 million related to monies paid in advance of litigation in occupancy tax proceedings in the cities of Santa Monica and San Francisco. In each case, we paid such amounts in order to be allowed to pursue litigation challenging whether we are required to pay hotel occupancy tax on the portion of the customer payment we retain as compensation and, if so, the actual amounts owed. We do not believe that the amounts we retain as compensation are subject to the cities' hotel occupancy tax ordinances. If we prevail in the litigation (including any appeal), the cities will be required to repay these amounts, plus interest. In December 2011, the city of Santa Monica returned the \$3 million in exchange for a letter of credit.

On February 17, 2012, the online travel companies, including Expedia, brought suit against the city of Portland and Multnomah County for a declaration that occupancy taxes are not due on the amounts they charge for their online services. Subsequent to the filing of the suit, the city and county sought to assess the online travel companies (approximately \$21 million for the Expedia companies with no disclosed supporting basis) and to require the payment of tax, interest and penalties before a legal determination is made. On March 22, 2012, the online travel companies obtained a temporary restraining order preventing the city and county from pursuing any assessment until the court has ruled on whether the online travel companies' lawsuit may proceed.

**NOTE 10 Related Party Transactions**

Mr. Diller, our Chairman of the Board of Directors and Senior Executive, through shares he owns beneficially as well as those subject to an irrevocable proxy granted by Liberty Interactive Corporation, controlled approximately 63% of the combined voting power of the outstanding Expedia capital stock as of March 31, 2012. As such, Mr. Diller effectively controls the outcome of all matters submitted to a vote or for the consent of our stockholders (other than with respect to the election by the holders of common stock of 25% of the members of our Board of Directors and matters as to which Delaware law requires a separate class vote). Upon Mr. Diller's permanent departure from Expedia, the irrevocable proxy would terminate and depending on the capitalization of Expedia at such time, Liberty could effectively control the voting

power of our capital stock.

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### **Notes to Consolidated Financial Statements - (Continued)**

In addition to serving as our Chairman and Senior Executive, Mr. Diller also serves as Chairman of the Board of Directors and Senior Executive at both IAC and TripAdvisor. Certain of our other executives also maintain roles with both IAC and TripAdvisor. Our certificate of incorporation provides that no officer or director of Expedia who is also an officer or director of IAC or of TripAdvisor will be liable to Expedia or its stockholders for breach of any fiduciary duty by reason of the fact that any such individual directs a corporate opportunity to IAC or TripAdvisor instead of Expedia, or does not communicate information regarding a corporate opportunity to Expedia because the officer or director has directed the corporate opportunity to IAC or TripAdvisor, which could have the effect of increasing the risk of conflicts of interest between the companies.

*TripAdvisor, Inc.* In connection with the spin-off, we entered into various agreements with TripAdvisor, a related party due to common ownership, including, among others, a separation agreement, a tax sharing agreement, an employee matters agreement and a transition services agreement. In addition, we will continue to work with TripAdvisor pursuant to various commercial agreements between subsidiaries of Expedia, on the one hand, and subsidiaries of TripAdvisor, on the other hand. The various commercial agreements, including click-based advertising agreements, content sharing agreements and display-based and other advertising agreements, have terms of up to one year. We recognized approximately \$2 million of revenue and expensed approximately \$51 million related to these various agreements with TripAdvisor during the three months ended March 31, 2012. In addition, we reclassified sales and marketing expense related to amounts we paid to TripAdvisor prior to the spin-off, which were previously eliminated in consolidation, to third party expenses for the three months ended March 31, 2011. Amounts payable to TripAdvisor were \$24 million and \$14 million as of March 31, 2012 and December 31, 2011 and were included in accounts payable, other on the consolidated balance sheet.

#### **Note 11 Segment Information**

We have two reportable segments: Leisure and Egencia. We determined our segments based on how our chief operating decision makers manage our business, make operating decisions and evaluate operating performance. Our primary operating metric is adjusted EBITDA. Adjusted EBITDA for our Leisure and Egencia segments includes allocations of certain expenses, primarily cost of revenue and facilities, and our Leisure segment includes the total costs of our global supply organizations as well as the realized foreign currency gains or losses related to the forward contracts hedging a component of our net merchant hotel revenue. We base the allocations primarily on transaction volumes and other usage metrics; this methodology is periodically evaluated and may change. We do not allocate certain shared expenses such as accounting, human resources, information technology and legal to our reportable segments. We include these expenses in Corporate.

Our Leisure segment provides a full range of travel and advertising services to our worldwide customers through a variety of brands including: Expedia.com and Hotels.com in the United States and localized Expedia and Hotels.com websites throughout the world, Expedia Affiliate Network, Hotwire.com, Venere, eLong and Classic Vacations. Our Egencia segment provides managed travel services to corporate customers in North America, Europe, and the Asia Pacific region.

Corporate also includes unallocated corporate functions and expenses. In addition, we record amortization of intangible assets and any related impairment, as well as stock-based compensation expense, restructuring charges, legal reserves, occupancy tax and other, and other items excluded from segment operating performance in Corporate. Such amounts are detailed in our segment reconciliation below.

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### Notes to Consolidated Financial Statements - (Continued)

The following tables present our segment information for the three months ended March 31, 2012 and 2011. As a significant portion of our property and equipment is not allocated to our operating segments and depreciation is not included in our segment measure, we do not report the assets by segment as it would not be meaningful. We do not regularly provide such information to our chief operating decision makers.

|                                                       | Three months ended March 31, 2012 |           |              |                   |
|-------------------------------------------------------|-----------------------------------|-----------|--------------|-------------------|
|                                                       | Leisure                           | Egencia   | Corporate    | Total             |
|                                                       | (In thousands)                    |           |              |                   |
| Revenue                                               | \$ 763,813                        | \$ 52,675 | \$           | \$ 816,488        |
| Adjusted EBITDA                                       | \$ 171,222                        | \$ 9,902  | \$ (79,306)  | \$ 101,818        |
| Depreciation                                          | (15,692)                          | (2,006)   | (16,616)     | (34,314)          |
| Amortization of intangible assets                     |                                   |           | (3,422)      | (3,422)           |
| Stock-based compensation                              |                                   |           | (16,951)     | (16,951)          |
| Legal reserves, occupancy tax and other               |                                   |           | 276          | 276               |
| Realized loss on revenue hedges                       | 1,276                             |           |              | 1,276             |
| Operating income (loss)                               | \$ 156,806                        | \$ 7,896  | \$ (116,019) | 48,683            |
| Other expense, net                                    |                                   |           |              | (21,856)          |
| Income from continuing operations before income taxes |                                   |           |              | 26,827            |
| Provision for income taxes                            |                                   |           |              | (5,240)           |
| Income from continuing operations                     |                                   |           |              | 21,587            |
| Discontinued operations, net of taxes                 |                                   |           |              | (23,889)          |
| Net loss                                              |                                   |           |              | (2,302)           |
| Net income attributable to noncontrolling interests   |                                   |           |              | (979)             |
| <b>Net loss attributable to Expedia, Inc.</b>         |                                   |           |              | <b>\$ (3,281)</b> |

|                                                       | Three months ended March 31, 2011 |           |              |            |
|-------------------------------------------------------|-----------------------------------|-----------|--------------|------------|
|                                                       | Leisure                           | Egencia   | Corporate    | Total      |
|                                                       | (In thousands)                    |           |              |            |
| Revenue                                               | \$ 685,672                        | \$ 42,163 | \$           | \$ 727,835 |
| Adjusted EBITDA                                       | \$ 149,995                        | \$ 7,738  | \$ (75,706)  | \$ 82,027  |
| Depreciation                                          | (12,764)                          | (2,003)   | (14,418)     | (29,185)   |
| Amortization of intangible assets                     |                                   |           | (5,834)      | (5,834)    |
| Stock-based compensation                              |                                   |           | (14,798)     | (14,798)   |
| Legal reserves, occupancy tax and other               |                                   |           | (2,358)      | (2,358)    |
| Realized loss on revenue hedges                       | 5,306                             |           |              | 5,306      |
| Operating income (loss)                               | \$ 142,537                        | \$ 5,735  | \$ (113,114) | 35,158     |
| Other expense, net                                    |                                   |           |              | (26,369)   |
| Income from continuing operations before income taxes |                                   |           |              | 8,789      |
| Provision for income taxes                            |                                   |           |              | (2,886)    |

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|                                                     |                  |
|-----------------------------------------------------|------------------|
| Income from continuing operations                   | 5,903            |
| Discontinued operations, net of taxes               | 46,306           |
| Net income                                          | 52,209           |
| Net income attributable to noncontrolling interests | (170)            |
| <b>Net income attributable to Expedia, Inc.</b>     | <b>\$ 52,039</b> |

**Table of Contents****Notes to Consolidated Financial Statements - (Continued)**

During the first quarter of 2012, we changed our allocation methodology for information technology expenses, which resulted in an increase of expenses at Corporate and a corresponding decrease in expenses being allocated to our Leisure and Egencia segments. In addition, in conjunction with certain organizational changes, we reclassified expenses attributed to our supplier payment group previously captured within Leisure to Corporate. We revised prior year adjusted EBITDA by segment to conform to our current year presentation. There was no impact on consolidated adjusted EBITDA as a result of these changes.

**NOTE 12 Guarantor and Non-Guarantor Supplemental Financial Information**

Condensed consolidating financial information of Expedia, Inc. (the Parent), our subsidiaries that are guarantors of our debt facility and instruments (the Guarantor Subsidiaries), and our subsidiaries that are not guarantors of our debt facility and instruments (the Non-Guarantor Subsidiaries) is shown below. The debt facility and instruments are guaranteed by certain of our wholly-owned domestic subsidiaries and rank equally in right of payment with all of our existing and future unsecured and unsubordinated obligations. The guarantees are full, unconditional, joint and several with the exception of certain customary automatic subsidiary release provisions. In this financial information, the Parent and Guarantor Subsidiaries account for investments in their wholly-owned subsidiaries using the equity method.

In connection with the spin-off, TripAdvisor Holdings, LLC and TripAdvisor LLC, both post-spin-off subsidiaries of TripAdvisor, were released from their guarantees of obligations under our existing debt facility and instruments. The discontinued operations of TripAdvisor and its subsidiaries have been presented within the following condensed consolidating financial statements within Guarantor Subsidiaries and Non-Guarantor Subsidiaries consistent with the classification in prior periods. In addition, in connection with the spin-off and the Notice of Redemption of the 8.5% Notes as described in Note 3 Acquisitions and Dispositions, such 8.5% Notes and the related deposit for the redemption were included within total current liabilities and total current assets of the Parent as of December 31, 2011.

**CONDENSED CONSOLIDATING STATEMENT OF OPERATION****Three months ended March 31, 2012**

|                                                         | Parent   | Guarantor<br>Subsidiaries | Non-Guarantor<br>Subsidiaries<br>(In thousands) | Eliminations | Consolidated |
|---------------------------------------------------------|----------|---------------------------|-------------------------------------------------|--------------|--------------|
| Revenue                                                 | \$       | \$ 723,520                | \$ 94,672                                       | \$ (1,704)   | \$ 816,488   |
| Costs and expenses:                                     |          |                           |                                                 |              |              |
| Cost of revenue                                         |          | 169,097                   | 30,678                                          | 323          | 200,098      |
| Selling and marketing                                   |          | 281,048                   | 98,141                                          | (2,117)      | 377,072      |
| Technology and content                                  |          | 82,733                    | 26,197                                          | (19)         | 108,911      |
| General and administrative                              |          | 51,725                    | 26,744                                          | 109          | 78,578       |
| Amortization of intangible assets                       |          | 1,760                     | 1,662                                           |              | 3,422        |
| Legal reserves, occupancy tax and other                 |          | (276)                     |                                                 |              | (276)        |
| Intercompany (income) expense, net                      |          | 142,747                   | (142,747)                                       |              |              |
| Operating income (loss)                                 |          | (5,314)                   | 53,997                                          |              | 48,683       |
| Other income (expense):                                 |          |                           |                                                 |              |              |
| Equity in pre-tax earnings of consolidated subsidiaries | 32,344   | 34,162                    |                                                 | (66,506)     |              |
| Other, net                                              | (20,806) | (137)                     | (913)                                           |              | (21,856)     |
| Total other income (expense), net                       | 11,538   | 34,025                    | (913)                                           | (66,506)     | (21,856)     |
| Income before income taxes                              | 11,538   | 28,711                    | 53,084                                          | (66,506)     | 26,827       |
| Provision for income taxes                              | 9,070    | 4,319                     | (18,629)                                        |              | (5,240)      |
| Income from continuing operations                       | 20,608   | 33,030                    | 34,455                                          | (66,506)     | 21,587       |

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|                                                           |                   |                  |                  |                    |                   |
|-----------------------------------------------------------|-------------------|------------------|------------------|--------------------|-------------------|
| Discontinued operations, net of taxes                     | (23,889)          |                  |                  |                    | (23,889)          |
| Net income (loss)                                         | (3,281)           | 33,030           | 34,455           | (66,506)           | (2,302)           |
| Net income attributable to noncontrolling interests       |                   |                  | (979)            |                    | (979)             |
| <b>Net income (loss) attributable to Expedia, Inc.</b>    | <b>\$ (3,281)</b> | <b>\$ 33,030</b> | <b>\$ 33,476</b> | <b>\$ (66,506)</b> | <b>\$ (3,281)</b> |
| Comprehensive income (loss) attributable to Expedia, Inc. | \$ (3,281)        | \$ 33,791        | \$ 47,057        | \$ (66,506)        | \$ 11,061         |

**Table of Contents****Notes to Consolidated Financial Statements - (Continued)****CONDENSED CONSOLIDATING STATEMENT OF OPERATION****Three months ended March 31, 2011**

|                                                         | Parent           | Guarantor<br>Subsidiaries | Non-Guarantor<br>Subsidiaries<br>(In thousands) | Eliminations        | Consolidated     |
|---------------------------------------------------------|------------------|---------------------------|-------------------------------------------------|---------------------|------------------|
| Revenue                                                 | \$               | \$ 641,458                | \$ 89,852                                       | \$ (3,475)          | \$ 727,835       |
| Costs and expenses:                                     |                  |                           |                                                 |                     |                  |
| Cost of revenue                                         |                  | 151,257                   | 24,298                                          | 55                  | 175,610          |
| Selling and marketing                                   |                  | 259,002                   | 95,402                                          | (3,496)             | 350,908          |
| Technology and content                                  |                  | 71,491                    | 15,316                                          |                     | 86,807           |
| General and administrative                              |                  | 52,007                    | 19,187                                          | (34)                | 71,160           |
| Amortization of intangible assets                       |                  | 1,274                     | 4,560                                           |                     | 5,834            |
| Legal reserves, occupancy tax and other                 |                  | 2,358                     |                                                 |                     | 2,358            |
| Intercompany (income) expense, net                      |                  | 122,189                   | (122,189)                                       |                     |                  |
| Operating income (loss)                                 |                  | (18,120)                  | 53,278                                          |                     | 35,158           |
| Other income (expense):                                 |                  |                           |                                                 |                     |                  |
| Equity in pre-tax earnings of consolidated subsidiaries | 20,284           | 49,017                    |                                                 | (69,301)            |                  |
| Other, net                                              | (20,795)         | (21,313)                  | 15,739                                          |                     | (26,369)         |
| Total other income (expense), net                       | (511)            | 27,704                    | 15,739                                          | (69,301)            | (26,369)         |
| Income before income taxes                              | (511)            | 9,584                     | 69,017                                          | (69,301)            | 8,789            |
| Provision for income taxes                              | 6,244            | 11,374                    | (20,504)                                        |                     | (2,886)          |
| Income from continuing operations                       | 5,733            | 20,958                    | 48,513                                          | (69,301)            | 5,903            |
| Discontinued operations, net of taxes                   | 46,306           | 49,431                    | 26,638                                          | (76,069)            | 46,306           |
| Net income                                              | 52,039           | 70,389                    | 75,151                                          | (145,370)           | 52,209           |
| Net income attributable to noncontrolling interests     |                  |                           | (170)                                           |                     | (170)            |
| <b>Net income attributable to Expedia, Inc.</b>         | <b>\$ 52,039</b> | <b>\$ 70,389</b>          | <b>\$ 74,981</b>                                | <b>\$ (145,370)</b> | <b>\$ 52,039</b> |
| Comprehensive income attributable to Expedia, Inc.      | \$ 52,039        | \$ 70,438                 | \$ 99,373                                       | \$ (145,370)        | \$ 76,480        |

**CONDENSED CONSOLIDATING BALANCE SHEET****March 31, 2012**

|                            | Parent     | Guarantor<br>Subsidiaries | Non-Guarantor<br>Subsidiaries<br>(In thousands) | Eliminations | Consolidated |
|----------------------------|------------|---------------------------|-------------------------------------------------|--------------|--------------|
| <b>ASSETS</b>              |            |                           |                                                 |              |              |
| Total current assets       | \$ 117,811 | \$ 2,472,721              | \$ 743,725                                      | \$ (749,615) | \$ 2,584,642 |
| Investment in subsidiaries | 3,947,822  | 1,107,135                 |                                                 | (5,054,957)  |              |

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|                                                   |                     |                     |                     |                       |                     |
|---------------------------------------------------|---------------------|---------------------|---------------------|-----------------------|---------------------|
| Intangible assets, net                            |                     | 639,536             | 99,322              |                       | 738,858             |
| Goodwill                                          |                     | 2,436,293           | 452,637             |                       | 2,888,930           |
| Other assets, net                                 | 5,601               | 459,004             | 141,148             |                       | 605,753             |
| <b>TOTAL ASSETS</b>                               | <b>\$ 4,071,234</b> | <b>\$ 7,114,689</b> | <b>\$ 1,436,832</b> | <b>\$ (5,804,572)</b> | <b>\$ 6,818,183</b> |
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>       |                     |                     |                     |                       |                     |
| Total current liabilities                         | \$ 658,528          | \$ 2,783,581        | \$ 309,695          | \$ (749,615)          | \$ 3,002,189        |
| Long-term debt                                    | 1,249,296           |                     |                     |                       | 1,249,296           |
| Other liabilities                                 | 7,911               | 379,066             | 24,222              |                       | 411,199             |
| Stockholders' equity                              | 2,155,499           | 3,952,042           | 1,102,915           | (5,054,957)           | 2,155,499           |
| <b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b> | <b>\$ 4,071,234</b> | <b>\$ 7,114,689</b> | <b>\$ 1,436,832</b> | <b>\$ (5,804,572)</b> | <b>\$ 6,818,183</b> |

**Table of Contents****Notes to Consolidated Financial Statements - (Continued)****CONDENSED CONSOLIDATING BALANCE SHEET****December 31, 2011**

|                                                   | <b>Parent</b>       | <b>Guarantor<br/>Subsidiaries</b> | <b>Non-Guarantor<br/>Subsidiaries<br/>(In thousands)</b> | <b>Eliminations</b>   | <b>Consolidated</b> |
|---------------------------------------------------|---------------------|-----------------------------------|----------------------------------------------------------|-----------------------|---------------------|
| <b>ASSETS</b>                                     |                     |                                   |                                                          |                       |                     |
| Total current assets                              | \$ 551,488          | \$ 1,538,509                      | \$ 644,825                                               | \$ (460,393)          | \$ 2,274,429        |
| Investment in subsidiaries                        | 3,891,811           | 1,126,412                         |                                                          | (5,018,223)           |                     |
| Intangible assets, net                            |                     | 634,581                           | 109,317                                                  |                       | 743,898             |
| Goodwill                                          |                     | 2,415,482                         | 461,819                                                  |                       | 2,877,301           |
| Other assets, net                                 | 5,587               | 465,473                           | 138,570                                                  |                       | 609,630             |
| <b>TOTAL ASSETS</b>                               | <b>\$ 4,448,886</b> | <b>\$ 6,180,457</b>               | <b>\$ 1,354,531</b>                                      | <b>\$ (5,478,616)</b> | <b>\$ 6,505,258</b> |
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>       |                     |                                   |                                                          |                       |                     |
| Total current liabilities                         | \$ 894,438          | \$ 1,906,349                      | \$ 212,963                                               | \$ (460,393)          | \$ 2,553,357        |
| Long-term debt                                    | 1,249,281           |                                   |                                                          |                       | 1,249,281           |
| Other liabilities                                 |                     | 378,729                           | 18,724                                                   |                       | 397,453             |
| Stockholders' equity                              | 2,305,167           | 3,895,379                         | 1,122,844                                                | (5,018,223)           | 2,305,167           |
| <b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b> | <b>\$ 4,448,886</b> | <b>\$ 6,180,457</b>               | <b>\$ 1,354,531</b>                                      | <b>\$ (5,478,616)</b> | <b>\$ 6,505,258</b> |

**CONDENSED CONSOLIDATING STATEMENT OF CASH FLOWS****Three months ended March 31, 2012**

|                                                                               | <b>Parent</b> | <b>Guarantor<br/>Subsidiaries<br/>(In thousands)</b> | <b>Non-Guarantor<br/>Subsidiaries</b> | <b>Consolidated</b> |
|-------------------------------------------------------------------------------|---------------|------------------------------------------------------|---------------------------------------|---------------------|
| <b>Operating activities:</b>                                                  |               |                                                      |                                       |                     |
| Net cash provided by operating activities from continuing operations          | \$            | \$ 832,140                                           | \$ 15,676                             | \$ 847,816          |
| <b>Investing activities:</b>                                                  |               |                                                      |                                       |                     |
| Capital expenditures, including internal-use software and website development |               | (41,917)                                             | (8,897)                               | (50,814)            |
| Purchases of investments                                                      |               | (226,114)                                            | (67,076)                              | (293,190)           |
| Sales and maturities of investments                                           |               | 196,501                                              | 44,140                                | 240,641             |
| Other, net                                                                    |               | 6,637                                                | (1,031)                               | 5,606               |
| Net cash used in investing activities from continuing operations              |               | (64,893)                                             | (32,864)                              | (97,757)            |
| <b>Financing activities:</b>                                                  |               |                                                      |                                       |                     |
| Treasury stock activity                                                       | (198,164)     |                                                      |                                       | (198,164)           |
| Payment of dividends to stockholders                                          | (12,204)      |                                                      |                                       | (12,204)            |

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|                                                                                |           |                   |                   |                     |
|--------------------------------------------------------------------------------|-----------|-------------------|-------------------|---------------------|
| Transfers (to) from related parties                                            | 171,176   | (171,176)         |                   |                     |
| Other, net                                                                     | 39,192    | (4,190)           | 115               | 35,117              |
| Net cash provided by (used in) financing activities from continuing operations |           | (175,366)         | 115               | (175,251)           |
| <b>Net cash provided by (used in) continuing operations</b>                    |           | <b>591,881</b>    | <b>(17,073)</b>   | <b>574,808</b>      |
| <b>Net cash used in discontinued operations</b>                                |           | <b>(7,607)</b>    |                   | <b>(7,607)</b>      |
| Effect of exchange rate changes on cash and cash equivalents                   |           | 13,153            | 3,020             | 16,173              |
| <b>Net increase (decrease) in cash and cash equivalents</b>                    |           | <b>597,427</b>    | <b>(14,053)</b>   | <b>583,374</b>      |
| Cash and cash equivalents at beginning of period                               |           | 357,252           | 331,882           | 689,134             |
| <b>Cash and cash equivalents at end of period</b>                              | <b>\$</b> | <b>\$ 954,679</b> | <b>\$ 317,829</b> | <b>\$ 1,272,508</b> |

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### Notes to Consolidated Financial Statements - (Continued)

#### CONDENSED CONSOLIDATING STATEMENT OF CASH FLOWS

Three months ended March 31, 2011

|                                                                                | Parent         | Guarantor<br>Subsidiaries | Non-Guarantor<br>Subsidiaries | Consolidated |
|--------------------------------------------------------------------------------|----------------|---------------------------|-------------------------------|--------------|
|                                                                                | (In thousands) |                           |                               |              |
| Operating activities:                                                          |                |                           |                               |              |
| Net cash provided by operating activities from continuing operations           | \$             | \$ 670,018                | \$ 22,633                     | \$ 692,651   |
| Investing activities:                                                          |                |                           |                               |              |
| Capital expenditures, including internal-use software and website development  |                | (41,576)                  | (4,510)                       | (46,086)     |
| Purchases of investments                                                       |                | (663,953)                 | (12,615)                      | (676,568)    |
| Sales and maturities of investments                                            |                | 289,689                   | 7,606                         | 297,295      |
| Other, net                                                                     |                | 844                       | 430                           | 1,274        |
| Net cash used in investing activities from continuing operations               |                | (414,996)                 | (9,089)                       | (424,085)    |
| Financing activities:                                                          |                |                           |                               |              |
| Treasury stock activity                                                        | (47,928)       |                           |                               | (47,928)     |
| Payment of dividends to stockholders                                           | (19,352)       |                           |                               | (19,352)     |
| Transfers (to) from related parties                                            | 62,927         | (62,927)                  |                               |              |
| Other, net                                                                     | 4,353          | (5,593)                   | 1,037                         | (203)        |
| Net cash provided by (used in) financing activities from continuing operations |                | (68,520)                  | 1,037                         | (67,483)     |
| Net cash provided by continuing operations                                     |                | 186,502                   | 14,581                        | 201,083      |
| Net cash provided by discontinued operations                                   |                | 40,202                    |                               | 40,202       |
| Effect of exchange rate changes on cash and cash equivalents                   |                | 3,308                     | 5,461                         | 8,769        |
| Net increase in cash and cash equivalents                                      |                | 230,012                   | 20,042                        | 250,054      |
| Cash and cash equivalents at beginning of period                               |                | 361,516                   | 259,683                       | 621,199      |
| Cash and cash equivalents at end of period                                     | \$             | \$ 591,528                | \$ 279,725                    | \$ 871,253   |

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### **Part I. Item 2. Management's Discussion and Analysis of Financial**

#### **Condition and Results of Operations**

##### **Forward-Looking Statements**

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These forward-looking statements reflect the views of our management regarding current expectations and projections about future events and are based on currently available information. Actual results could differ materially from those contained in these forward-looking statements for a variety of reasons, including, but not limited to, those discussed in our Annual Report on Form 10-K for the year ended December 31, 2011, Part I, Item 1A, Risk Factors, as well as those discussed elsewhere in this report. Other unknown or unpredictable factors also could have a material adverse effect on our business, financial condition and results of operations. Accordingly, readers should not place undue reliance on these forward-looking statements. The use of words such as anticipates, estimates, expects, intends, plans and believes, among others, generally identify forward-looking statements; however, these words are not the exclusive means of identifying such statements. In addition, any statements that refer to expectations, projections or other characterizations of future events or circumstances are forward-looking statements. These forward-looking statements are inherently subject to uncertainties, risks and changes in circumstances that are difficult to predict. We are not under any obligation to, and do not intend to, publicly update or review any of these forward-looking statements, whether as a result of new information, future events or otherwise, even if experience or future events make it clear that any expected results expressed or implied by those forward-looking statements will not be realized. Please carefully review and consider the various disclosures made in this report and in our other reports filed with the Securities and Exchange Commission (SEC) that attempt to advise interested parties of the risks and factors that may affect our business, prospects and results of operations.

The information included in this management's discussion and analysis of financial condition and results of operations should be read in conjunction with our consolidated financial statements and the notes included in this Quarterly Report, and the audited consolidated financial statements and notes and Management's Discussion and Analysis of Financial Condition and Results of Operations contained in our Annual Report on Form 10-K for the year ended December 31, 2011.

##### **Overview**

Expedia, Inc. is an online travel company, empowering business and leisure travelers with the tools and information they need to efficiently research, plan, book and experience travel. We have created a global travel marketplace used by a broad range of leisure and corporate travelers, offline retail travel agents and travel service providers. We make available, on a stand-alone and package basis, travel products and services provided by numerous airlines, lodging properties, car rental companies, destination service providers, cruise lines and other travel product and service companies. We also offer travel and non-travel advertisers access to a potential source of incremental traffic and transactions through our various media and advertising offerings on our transaction-based websites.

Our portfolio of brands includes Expedia.com®, Hotels.com®, Hotwire.com™, Expedia Affiliate Network (EAN), Classic Vacations, Expedia Local Expert™, Expedia® CruiseShipCenters®, Egencia™, eLong™, and Venere Net SpA (Venere). In addition, many of these brands have related international points of sale. For additional information about our portfolio of brands, see Portfolio of Brands in Part I, Item 1, Business, in our Annual Report on Form 10-K for the year ended December 31, 2011.

On December 20, 2011, following the close of trading on the Nasdaq Stock Market, we completed the spin-off of TripAdvisor, Inc. (TripAdvisor), which consisted of the domestic and international operations previously associated with our TripAdvisor Media Group, to Expedia stockholders. We refer to this transaction as the spin-off. Immediately prior to the spin-off, Expedia effected a one-for-two reverse stock split.

All percentages within this section are calculated on actual, unrounded numbers.

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### ***Trends***

The travel industry, including offline agencies, online agencies and other suppliers of travel products and services, has historically been characterized by intense competition, as well as rapid and significant change. Generally, 2011 represented a year of gradual improvement for the travel industry. However, natural disasters, such as the earthquake and tsunami in Japan, political and social unrest in the Middle East and North Africa, the rising price of oil, and ongoing sovereign debt and economic issues in several European countries, all contribute to a somewhat uncertain forward environment for the travel industry.

### ***Online Travel***

Increased usage and familiarity with the internet have driven rapid growth in online penetration of travel expenditures. According to PhoCusWright, an independent travel, tourism and hospitality research firm, in 2011, approximately 54% of U.S. leisure, unmanaged and corporate travel expenditures occurred online, compared with approximately 39% of European travel. Online penetration in the Asia Pacific region is estimated to be over 20%, lagging behind that of Europe. These penetration rates have increased over the past few years, and are expected to continue growing. This significant growth has attracted many competitors to online travel. This competition has intensified in recent years, and the industry is expected to remain highly competitive for the foreseeable future. In addition to the growth of online travel agencies, airlines and lodging companies have aggressively pursued direct online distribution of their products and services, and supplier growth outpaced online agency growth for several years. Competitive entrants such as metasearch companies have in some cases been able to introduce differentiated features and content compared with the legacy online travel agency companies. New models, such as daily deals and private sale sites have also begun proliferating. We have a number of daily deals offered on our retail websites as well as deal specific offerings such as Hotwire's Travel-Ticker, and a partnership with Groupon called Groupon Getaways with Expedia. In addition, we have seen increased interest in the online travel industry from search engine companies as evidenced by recent innovations and proposed and actual acquisitions by companies such as Google and Microsoft.

The online travel industry has also seen the development of alternative business models and variations in the timing of payment by travelers and to suppliers, which in some cases place pressure on historical business models. In particular, the agency hotel model has seen rapid adoption in Europe. Expedia has both a merchant and an agency hotel offer for our hotel supply partners and we expect our use of these models to continue to evolve.

Intense competition has also historically led to aggressive marketing spend by the travel suppliers and intermediaries, and a meaningful reduction in our overall marketing efficiencies and operating margins. We manage our selling and marketing spending on a brand basis at the local or regional level, making decisions in each market that we think are appropriate based on the relative growth opportunity, the expected returns and the competitive environment. In certain cases, we are pursuing and expect to continue to pursue long-term growth opportunities for which our marketing efficiency is lower than that for our consolidated business but for which we still believe the opportunity to be attractive. However, we believe that over the long-term we can manage our sales and marketing expense to be roughly in line with revenue growth.

### ***Hotel***

We generate the majority of our revenue through the marketing and distribution of hotel rooms (stand-alone and package bookings). Our relationships and negotiated economics with our hotel supply partners have remained broadly stable in the past few years. We have, however, implemented new customer loyalty programs and have eliminated or reduced some fees in that timeframe and, as such, the margin of revenue we earn per booking has declined. Over the course of the last two years, occupancies and average daily rates (ADRs) in the lodging industry have generally improved in a gradually improving overall travel environment. From a supply perspective, there is very little new, net hotel supply being added in the U.S. lodging market with large chains focusing their development opportunities in international markets. This may help hoteliers with their objective of continuing to grow their ADRs and could lead to pressure in negotiations with hoteliers and may ultimately lead to pressure on terms for us and our OTA competitors. In international markets, hotel supply is being added at a much faster rate as hotel owners and operators try to take advantage of opportunities in faster growing regions such as China and India, among others. We have had success adding supply to our marketplace with over 150,000 hotels as of the end of the first quarter of 2012 representing growth of 11%. In addition, our room night growth has been healthy, with room nights growing 14% in 2010, 18% in 2011 and 24% for the first quarter of 2012. ADRs for rooms booked on Expedia sites grew 1% in 2010 and 5% in 2011, while they were flat year-over-year for the first quarter of 2012.

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### ***Air***

The airline sector in particular has historically experienced significant turmoil. In recent years, there has been increased air carrier consolidation, generally resulting in lower overall capacity and higher fares. In addition, air carriers have made significant efforts to keep seat capacity relatively low in order to ensure that demand for seats remains high and that flights are as full as possible. Reduced seating capacities are generally negative for Expedia as there is less air supply available on our websites, and in turn less opportunity to facilitate hotel rooms, car rental and other services on behalf of air travelers. Ticket prices on Expedia sites grew 11% in 2011 and 7% in the first quarter of 2012. We are encountering significant pressure on air remuneration as certain supply agreements renew, and as air carriers and global distribution system ( GDS ) intermediaries re-negotiate their long-term agreements.

In part as a result of sharply rising average ticket prices, our ticket volumes decreased by 8% in 2011 after having grown by 11% in 2010. Air ticket volumes grew 5% in the first quarter of 2012, largely due to air ticket sales of a major U.S. carrier, which were absent in the first quarter of 2011 due to a commercial disagreement.

From a product perspective, over 70% of our revenue comes from transactions involving the booking of hotel reservations, with just over 10% of our revenue derived from the sale of airline tickets. We believe that the hotel product is the most profitable of the products we distribute and represents our best overall growth opportunity.

### ***Growth Strategy***

*Product Innovation.* Each of our leading brands was a pioneer in online travel and has been responsible for driving key innovations in the space over the past two decades. They each operate a dedicated technology team, which drives innovations that make researching and shopping for travel increasingly easier and helps customers find and book the best possible travel options. In the past several years, we made key investments in technology, including significant development of our technological platforms that makes it possible for us to deliver innovations at a faster pace. For example, we launched our new Hotels.com global platform in the first quarter of 2010, enabling us to significantly increase the innovation cycle for that brand. Since then, we have been successful in improving conversion and driving much faster growth rates for the Hotels.com brand. We are in the midst of a similar transformation for our Expedia brand, having rolled out its new hotel platform in the second half of 2011, with expectations that the new air and package platforms will be launched in 2012.

*Global Expansion.* Our Expedia, Hotels.com, Egencia, EAN, and Hotwire brands operate both domestically and through international points of sale, including in Europe, Asia Pacific, Canada and Latin America. We own a majority share of eLong, which is the second largest online travel company in China. We also own Venere, a European brand, which focuses on marketing hotel rooms in Europe. Egencia, our corporate travel business, operates in 46 countries around the world and continues to expand aggressively. We also partner in a 50/50 joint venture with AirAsia a low cost carrier serving the Asia-Pacific region to jointly grow an online travel agency business. Although the results for the joint venture are not consolidated in our financial statements, we consider this business to be a key part of our Asia Pacific strategy. In 2011, approximately 39% of our worldwide gross bookings and 42% of worldwide revenue were international up from 22% for both worldwide gross bookings and revenue in 2005. In the first quarter of 2012, 39% of our gross bookings and 40% of our revenue were international. We have a stated goal of driving more than half of our gross bookings and revenue through international points of sale.

In expanding our global reach, we leverage significant investments in technology, operations, brand building, supplier relationships and other initiatives that we have made since the launch of Expedia.com in 1996. We intend to continue leveraging these investments when launching additional points of sale in new countries, introducing new website features, adding supplier products and services including new business model offerings, as well as proprietary and user-generated content for travelers.

Our scale of operations enhances the value of technology innovations we introduce on behalf of our travelers and suppliers. We believe that our size and scale affords the company the ability to negotiate competitive rates with our supply partners, provide breadth of choice and travel deals to our traveling customers through an increasingly larger supply portfolio

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and creates opportunities for new value added offers for our customers such as our loyalty programs. The size of Expedia's worldwide traveler base makes our sites an increasingly appealing channel for travel suppliers to reach customers. In addition, the sheer size of our user base and search query volume allows us to test new technology very quickly in order to determine which innovations are most likely to improve the travel research and booking process, and then roll those features out to our worldwide audience in order to drive improvements to conversion.

*New Channel Penetration.* Today, the vast majority of online travel bookings are generated through typical desktop and laptop computers. However, recent technological innovations and developments are creating new opportunities including travel bookings made through mobile devices. In the past few years, each of our brands made significant progress creating new mobile websites and mobile applications that are receiving strong reviews and solid download trends. We own a leading travel application company called Mobiata which is responsible for several top travel applications, such as FlightTrack, FlightTrack Pro and FlightBoard, and is now creating new mobile applications for our Expedia brand, most recently launching the mobile Expedia Hotels application for both the iPhone and the iPad. We believe mobile bookings present an opportunity for incremental growth as they are typically completed within one day of the travel or stay which is a much shorter booking window than we have historically experienced via more traditional online booking methods. We are also working with suppliers on specific mobile offerings which can represent a unique value proposition and offer customers room nights for as much as a 50% discount from retail rates.

Other recent developments in new channels include the proliferation of the daily deals space for which we have multiple efforts. For example, our Expedia brand has an exclusive partnership with Groupon, Groupon Getaways with Expedia, where we work with suppliers to offer consumers deeply discounted travel opportunities on a limited basis. We believe this may also represent incremental travel bookings as it typically represents an impulse purchase compared to historical travel purchasing activity which tends to be a highly considered and deliberate transaction. Our Hotwire brand also operates the Travel-Ticker brand which sources and markets deep discount travel. Virtually all of our leisure brands have efforts related to the daily deals or deep discount space.

Many of our brands are also actively participating in Facebook, Twitter and other social channels and we anticipate the importance of these channels to consumers and to our industry to increase over time. It is our intention to grow our social efforts alongside this trend.

### ***Seasonality***

We generally experience seasonal fluctuations in the demand for our travel products and services. For example, traditional leisure travel bookings are generally the highest in the first three quarters as travelers plan and book their spring, summer and holiday travel. The number of bookings typically decreases in the fourth quarter. Because revenue in the merchant business is generally recognized when the travel takes place rather than when it is booked, revenue typically lags bookings by several weeks or longer. The seasonal revenue impact is exacerbated with respect to income by the more stable nature of our fixed costs. As a result, revenue and income are typically the lowest in the first quarter and highest in the third quarter. Additionally, prior to the spin-off, TripAdvisor typically comprised a larger relative portion of our revenue and income during the first quarter. Thus, following the spin-off the seasonal impact on our business will be more pronounced, particularly in the first quarter, as the bookings versus recognition of revenue time lag under the merchant hotel business represents a larger portion of our operating results without TripAdvisor. The continued growth of our international operations or a change in our product mix may influence the typical trend of the seasonality in the future.

### **Critical Accounting Policies and Estimates**

Critical accounting policies and estimates are those that we believe are important in the preparation of our consolidated financial statements because they require that we use judgment and estimates in applying those policies. We prepare our consolidated financial statements and accompanying notes in accordance with generally accepted accounting principles in the United States (GAAP). Preparation of the consolidated financial statements and accompanying notes requires that we make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities as of the date of the consolidated financial statements as well as revenue and expenses during the periods reported. We base our estimates on historical experience, where applicable, and other assumptions that we believe are reasonable under the circumstances. Actual results may differ from our estimates under different assumptions or conditions.

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There are certain critical estimates that we believe require significant judgment in the preparation of our consolidated financial statements. We consider an accounting estimate to be critical if:

It requires us to make an assumption because information was not available at the time or it included matters that were highly uncertain at the time we were making the estimate; and

Changes in the estimate or different estimates that we could have selected may have had a material impact on our financial condition or results of operations.

For additional information about our critical accounting policies and estimates, see the disclosure included in our Annual Report on Form 10-K for the year ended December 31, 2011.

## **New Accounting Pronouncements**

For a discussion of new accounting pronouncements, see Note 2 – Summary of Significant Accounting Policies in the notes to the consolidated financial statements.

## **Occupancy Taxes**

We are currently involved in 49 lawsuits brought by or against states, cities and counties over issues involving the payment of hotel occupancy taxes. We continue to defend these lawsuits vigorously. With respect to the principal claims in these matters, we believe that the ordinances at issue do not apply to the services we provide, namely the facilitation of hotel reservations, and, therefore, that we do not owe the taxes that are claimed to be owed. We believe that the ordinances at issue generally impose occupancy and other taxes on entities that own, operate or control hotels (or similar businesses) or furnish or provide hotel rooms or similar accommodations.

Recent developments include:

*Branson, Missouri Litigation.* On January 28, 2012, the court granted the defendant online travel companies' motion to dismiss holding that online travel companies are not subject to hotel occupancy tax. The city has appealed.

*Cities of Goodlettsville and Brentwood, Tennessee Litigation.* On February 21, 2012, the court granted the online travel companies' motion for summary judgment and denied the cities' motion for summary judgment, and held that online travel companies are not liable for occupancy taxes.

*City of Bowling Green, Kentucky Litigation.* On February 15, 2012, the Kentucky Supreme Court denied the city of Bowling Green's motion for discretionary review of the Court of Appeal's decision that online travel companies are not liable for hotel occupancy tax.

*City of Birmingham, Alabama Litigation.* On April 13, 2012, the Alabama Supreme Court affirmed the lower court's grant of summary judgment in favor of the online travel companies and held that hotel occupancy taxes are not due from online travel companies.

*Leon County, Florida et al. Litigation.* On April 19, 2012, the court granted the online travel companies' motion for summary judgment and denied the counties' motion for summary judgment.

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*City of Philadelphia Litigation.* On February 2, 2012, the Commonwealth Court of Pennsylvania affirmed the lower court decision and held that hotel occupancy taxes are not due from Expedia.

*City of Portland Litigation.* On February 17, 2012, the online travel companies brought suit against the city of Portland and Multnomah County for a declaration that occupancy taxes are not due on the amounts they charge for their online services. Subsequent to the filing of the suit, the city and county sought to assess the online travel

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companies (approximately \$21 million for the Expedia companies with no disclosed supporting basis) and to require the payment of tax, interest and penalties before a legal determination is made. On March 22, 2012, the online travel companies obtained a temporary restraining order preventing the city and county from pursuing any assessment until the court has ruled on whether the online travel companies' lawsuit may proceed.

For additional information on these and other legal proceedings, see Part II, Item 1, Legal Proceedings.

We have established a reserve for the potential settlement of issues related to hotel occupancy tax litigation, consistent with applicable accounting principles and in light of all current facts and circumstances, in the amount of \$31 million as of March 31, 2012, which includes amounts expected to be paid in connection with the developments described above, and \$32 million as of December 31, 2011. In addition, as of March 31, 2012 and December 31, 2011, we have also accrued \$1 million and \$10 million related to court decisions and the potential and final settlement of issues related to hotel occupancy taxes.

Certain jurisdictions may require us to pay tax assessments, including occupancy tax assessments, prior to contesting any such assessments. This requirement is commonly referred to as "pay-to-play." Payment of these amounts is not an admission that the taxpayer believes it is subject to such taxes. During 2009, we expensed \$48 million related to monies paid in advance of litigation in occupancy tax proceedings in the city of San Francisco. During 2010, we expensed \$3 million related to monies paid in advance of litigation in occupancy tax proceedings in the city of Santa Monica; these funds were returned to us by the city in December 2011 in exchange for a letter of credit. We do not believe that the amounts we retain as compensation are subject to the cities' hotel occupancy tax ordinances. If we prevail in the litigation, for which a pay-to-play payment was made, the jurisdiction collecting the payment will be required to repay such amounts, plus interest. However, any significant pay-to-play payment or litigation loss could negatively impact our liquidity.

In addition, certain jurisdictions, including the states of New York, North Carolina and Minnesota, the city of New York, and the District of Columbia, have enacted legislation seeking to tax online travel company services as part of sales taxes for hotel occupancy.

## **Segments**

We have two reportable segments: Leisure, and Egencia. We determined our segments based on how our chief operating decision makers manage our business, make operating decisions and evaluate operating performance.

Our Leisure segment provides a full range of travel and advertising services to our worldwide customers through a variety of brands including: Expedia.com and Hotels.com in the United States and localized Expedia and Hotels.com websites throughout the world, EAN, Hotwire.com, Venere, eLong and Classic Vacations. Our Egencia segment provides managed travel services to corporate customers in North America, Europe, and the Asia Pacific region.

## **Operating Metrics**

Our operating results are affected by certain metrics, such as gross bookings and revenue margin, which we believe are necessary for understanding and evaluating us. Gross bookings represent the total retail value of transactions booked for both agency and merchant transactions, recorded at the time of booking reflecting the total price due for travel by travelers, including taxes, fees and other charges, and are generally reduced for cancellations and refunds. As travelers have increased their use of the internet to book travel arrangements, we have generally seen our gross bookings increase, reflecting the growth in the online travel industry, our organic market share gains and our business acquisitions. Revenue margin is defined as revenue as a percentage of gross bookings.

**Table of Contents*****Gross Bookings and Revenue Margin***

|                              | Three months ended March 31, |          | % Change |
|------------------------------|------------------------------|----------|----------|
|                              | 2012                         | 2011     |          |
|                              | (\$ in millions)             |          |          |
| <b><u>Gross Bookings</u></b> |                              |          |          |
| Leisure                      | \$ 7,666                     | \$ 6,653 | 15%      |
| Egencia                      | 755                          | 642      | 18%      |
| Total gross bookings         | \$ 8,421                     | \$ 7,295 | 15%      |
| <b><u>Revenue Margin</u></b> |                              |          |          |
| Leisure                      | 10.0%                        | 10.3%    |          |
| Egencia                      | 7.0%                         | 6.6%     |          |
| Total revenue margin         | 9.7%                         | 10.0%    |          |

The increase in worldwide gross bookings for the three months ended March 31, 2012, as compared to the same period in 2011, was primarily due to a 24% increase in hotel room nights through accelerated growth in all Leisure brands except Expedia.

The decrease in revenue margin for the three months ended March 31, 2012, as compared to the same period in 2011, was primarily due to lower net air supplier economics, rising average air ticket prices as our remuneration generally does not vary with the price of the ticket and changes in our hotel product mix, partially offset by growth in our higher margin hotel business.

**Results of Operations*****Revenue***

|                           | Three months ended March 31, |        | % Change |
|---------------------------|------------------------------|--------|----------|
|                           | 2012                         | 2011   |          |
|                           | (\$ in millions)             |        |          |
| <b>Revenue by Segment</b> |                              |        |          |
| Leisure                   | \$ 763                       | \$ 686 | 11%      |
| Egencia                   | 53                           | 42     | 25%      |
| Total revenue             | \$ 816                       | \$ 728 | 12%      |

Revenue increased for the three months ended March 31, 2012, compared to the same period in 2011, primarily due to an increase in worldwide hotel revenue within our Leisure segment.

Worldwide hotel revenue increased 18% for the three months ended March 31, 2012, compared to the same period in 2011. The increase was primarily due to a 24% increase in room nights stayed, partially offset by a 6% decrease in revenue per room night. Revenue per room night decreased primarily due to changes in our hotel product mix, discounting at the Hotwire brand, accruals for loyalty programs at Expedia and Hotels.com and impacts of foreign currency.

Worldwide air revenue decreased 17% for the three months ended March 31, 2012, compared to the same period in 2011, due to a 20% decrease in revenue per air ticket, partially offset by a 5% increase in air tickets sold. Revenue per air ticket declined due to lower net supplier economics, partially offset by certain regional and interline consumer booking fees. The increase in air ticket sold was due to availability of American Airlines tickets for the duration of the first quarter of 2012 that were not available to leisure consumers for the duration of the first quarter of 2011, partially offset by a 7% increase in average air ticket prices.



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The remaining worldwide revenue, other than hotel and air discussed above, increased by 15% for the three months ended March 31, 2012, compared to the same period in 2011, primarily due to an increase in car revenue, advertising and media revenue and fees related to our corporate travel business.

In addition to the above segment and product revenue discussion, our revenue by business model is as follows:

|                                         | Three months ended March 31, |        | % Change |
|-----------------------------------------|------------------------------|--------|----------|
|                                         | 2012                         | 2011   |          |
|                                         | (\$ in millions)             |        |          |
| <b><u>Revenue by Business Model</u></b> |                              |        |          |
| Merchant                                | \$ 603                       | \$ 520 | 16%      |
| Agency                                  | 182                          | 181    | 1%       |
| Advertising and media                   | 31                           | 27     | 14%      |
| Total revenue                           | \$ 816                       | \$ 728 | 12%      |

Merchant revenue increased for the three months ended March 31, 2012, compared to the same period in 2011, due to the increase in merchant hotel revenue primarily driven by an increase in room nights stayed.

Agency revenue remained relatively flat for the three months ended March 31, 2012, compared to the same period in 2011, as the growth in our agency hotel business and corporate travel business was mostly offset by a decline in agency air revenue.

***Cost of Revenue***

|                        | Three months ended March 31, |        | % Change |
|------------------------|------------------------------|--------|----------|
|                        | 2012                         | 2011   |          |
|                        | (\$ in millions)             |        |          |
| Customer operations    | \$ 97                        | \$ 83  | 17%      |
| Credit card processing | 62                           | 54     | 14%      |
| Data center and other  | 41                           | 39     | 7%       |
| Total cost of revenue  | \$ 200                       | \$ 176 | 14%      |
| % of revenue           | 24.5%                        | 24.1%  |          |

Cost of revenue primarily consists of (1) customer operations, including our customer support and telesales as well as fees to air ticket fulfillment vendors, (2) credit card processing, including merchant fees, charge backs and fraud, and (3) other costs, primarily including data center costs to support our websites, destination supply, and stock-based compensation.

During the three months ended March 31, 2012, the primary drivers of the increase in cost of revenue expense were higher credit card processing costs related to our merchant bookings growth as well as higher personnel expenses driven by additional headcount to support our global customer operations, partially offset by lower debit card fees and an increase in credit card rebates.

***Selling and Marketing***

|                | Three months ended March 31, |        | % Change |
|----------------|------------------------------|--------|----------|
|                | 2012                         | 2011   |          |
|                | (\$ in millions)             |        |          |
| Direct costs   | \$ 282                       | \$ 269 | 5%       |
| Indirect costs | 95                           | 82     | 16%      |

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|                             |        |        |    |
|-----------------------------|--------|--------|----|
| Total selling and marketing | \$ 377 | \$ 351 | 7% |
|-----------------------------|--------|--------|----|

% of revenue

46.2%

48.2%

Selling and marketing expense primarily relates to direct costs, including traffic generation costs from search engines and internet portals, television, radio and print spending, private label and affiliate program commissions, public relations and other costs. The remainder of the expense relates to indirect costs, including personnel and related overhead in our global supply organization, Egencia and various Leisure brands and stock-based compensation costs.

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Selling and marketing expenses increased \$26 million during the three months ended March 31, 2012, compared to the same period in 2011, driven by increases in affiliate marketing expenses at EAN, offline marketing expenses at Hotwire and Hotels.com as well as higher personnel expenses driven by additional headcount across several brands and our supply organization, partially offset by lower online marketing expenses at our Expedia brand.

### Technology and Content

|                                                    | Three months ended March 31, |       | % Change |
|----------------------------------------------------|------------------------------|-------|----------|
|                                                    | 2012                         | 2011  |          |
|                                                    | (\$ in millions)             |       |          |
| Personnel and overhead                             | \$ 61                        | \$ 46 | 32%      |
| Depreciation and amortization of technology assets | 23                           | 19    | 20%      |
| Other                                              | 25                           | 22    | 16%      |
| Total technology and content                       | \$ 109                       | \$ 87 | 25%      |
| % of revenue                                       | 13.3%                        | 11.9% |          |

Technology and content expense includes product development and content expense, as well as information technology costs to support our infrastructure, back-office applications and overall monitoring and security of our networks, and is principally comprised of personnel and overhead, depreciation and amortization of technology assets including hardware, and purchased and internally developed software, and other costs including licensing and maintenance expense and stock-based compensation.

The increase of \$22 million in technology and content expense during the three months ended March 31, 2012, compared to the same period in 2011, was primarily due to increased personnel costs for increased headcount to support our Expedia brand, supply organization and corporate technology function as well as increased depreciation and amortization of technology assets.

### General and Administrative

|                                  | Three months ended March 31, |       | % Change |
|----------------------------------|------------------------------|-------|----------|
|                                  | 2012                         | 2011  |          |
|                                  | (\$ in millions)             |       |          |
| Personnel and overhead           | \$ 50                        | \$ 42 | 18%      |
| Professional fees and other      | 29                           | 29    | (1%)     |
| Total general and administrative | \$ 79                        | \$ 71 | 10%      |
| % of revenue                     | 9.6%                         | 9.8%  |          |

General and administrative expense consists primarily of personnel-related costs, including our executive leadership, finance, legal and human resource functions as well as fees for external professional services including legal, tax and accounting, and other costs including stock-based compensation.

The \$8 million increase in general and administrative expense during the three months ended March 31, 2012, compared to the same period in 2011, was due primarily to higher personnel expenses resulting from an increase in headcount.

**Table of Contents*****Amortization of Intangible Assets***

|                                   | Three months ended March 31, |      | % Change |
|-----------------------------------|------------------------------|------|----------|
|                                   | 2012                         | 2011 |          |
|                                   | (\$ in millions)             |      |          |
| Amortization of intangible assets | \$ 3                         | \$ 6 | (41%)    |
| % of revenue                      | 0.4%                         | 0.8% |          |

Amortization for the three months ended March 31, 2012 included an approximate \$2 million reduction related to a change in the estimated value of contingent purchase consideration for one of our prior acquisitions.

***Legal Reserves, Occupancy Tax and Other***

Legal reserves, occupancy tax and other consists of changes in our reserves for court decisions and the potential and final settlement of issues related to hotel occupancy taxes, expenses recognized related to monies paid in advance of occupancy tax proceedings ( pay-to-play ) as well as certain other legal reserves. Legal reserves, occupancy tax and other was a gain of less than \$1 million for the three months ended March 31, 2012 compared to expense of approximately \$2 million for the three months ended March 31, 2011.

***Operating Income***

|                  | Three months ended March 31, |       | % Change |
|------------------|------------------------------|-------|----------|
|                  | 2012                         | 2011  |          |
|                  | (\$ in millions)             |       |          |
| Operating income | \$ 49                        | \$ 35 | 38%      |
| % of revenue     | 6.0%                         | 4.8%  |          |

Operating income increased for the three months ended March 31, 2012, compared to the same period in 2011, primarily due to a growth in revenue in excess of operating expenses.

***Interest Income and Expense***

|                  | Three months ended March 31, |      | % Change |
|------------------|------------------------------|------|----------|
|                  | 2012                         | 2011 |          |
|                  | (\$ in millions)             |      |          |
| Interest income  | \$ 6                         | \$ 3 | 72%      |
| Interest expense | (21)                         | (23) | (5%)     |

Interest income increased for the three months ended March 31, 2012, compared to the same period in 2011, primarily due to a higher rate of return on cash, cash equivalent and investment balances as well as higher average balances.

***Other, Net***

Other, net changed from a loss of \$7 million for the three months ended March 31, 2011 to a loss of \$6 million for the three months ended March 31, 2012 primarily due to lower net foreign exchange rate losses, partially offset by an increase in equity method operating losses.

**Table of Contents*****Provision for Income Taxes***

|                            | Three months ended March 31, |       |          |
|----------------------------|------------------------------|-------|----------|
|                            | 2012                         | 2011  | % Change |
|                            | (\$ in millions)             |       |          |
| Provision for income taxes | \$ 5                         | \$ 3  | 82%      |
| Effective tax rate         | 19.5%                        | 32.8% |          |

We determine our provision for income taxes for interim periods using an estimate of our annual effective rate. We record any changes to the estimated annual rate in the interim period in which the change occurs, including discrete tax items.

The decrease in the effective rate for the three months ended March 31, 2012 as compared to the same period in 2011 was primarily due to a release of accruals related to uncertain tax positions as well as an increase in estimated earnings in jurisdictions outside of the United States.

Our effective tax rate was 19.5% for the three months ended March 31, 2012, which was lower than the 35% federal statutory rate primarily due to estimated earnings in jurisdictions outside the United States and accruals related to uncertain tax positions, partially offset by state income taxes. Our effective tax rate was 32.8% for the three months ended March 31, 2011, which was lower than the 35% federal statutory rate primarily due to estimated earnings in jurisdictions outside the United States, partially offset by state income taxes and accruals related to uncertain tax positions.

***Discontinued Operations, Net of Taxes***

During the three months ended March 31, 2012, we incurred a loss from early extinguishment of our 8.5% senior notes due 2016 (the 8.5% Notes ) resulting directly from the spin-off of TripAdvisor. The pre-tax loss was approximately \$38 million (or \$24 million net of tax), which included an early redemption premium of \$33 million and the write-off of \$5 million of unamortized debt issuance and discount costs. This loss was recorded within discontinued operations in the first quarter of 2012, as that was the period in which the 8.5% Notes were legally extinguished. For additional information, see Note 3 Acquisitions and Dispositions in the notes to the consolidated financial statements. Discontinued operations also includes the results of operations of TripAdvisor for the three months ended March 31, 2011, the reclassification of expense related to the obligation to fund a charitable foundation that was assumed by TripAdvisor in conjunction with the spin-off as well as interest expense and amortization of debt issuance costs and discount related to 8.5% Notes which were redeemed in connection with the spin-off.

**Financial Position, Liquidity and Capital Resources**

Our principal sources of liquidity are cash flows generated from operations; our cash and cash equivalents and short-term investment balances, which were \$2.0 billion and \$1.3 billion at March 31, 2012 and December 31, 2011, including \$304 million and \$302 million of cash and short-term investment balances of majority-owned subsidiaries as well as \$152 million and \$131 million held in foreign subsidiaries related to earnings indefinitely invested outside the United States; and our \$750 million revolving credit facility. As of March 31, 2012, \$728 million was available under the facility representing the total \$750 million facility less \$22 million of outstanding stand-by letters of credit. The revolving credit facility bears interest based on the Company's credit ratings, with drawn amounts bearing interest at LIBOR plus 150 basis points, and the commitment fee on undrawn amounts at 22.5 basis points as of March 31, 2012.

The indenture governing our \$400 million aggregate principal amount of 8.5% Notes contained certain covenants that could have restricted implementation of the spin-off. On December 20, 2011, prior to consummation of the spin-off, we gave Notice of Redemption to the bondholders, the effect of which was the bonds became due and payable on the redemption date at the redemption price. The redemption date is defined as 30 days after the Notice of Redemption is given. In order to complete the Notice of Redemption, we were required to irrevocably deposit, with the Trustee, funds sufficient to pay the redemption price plus accrued interest on the 8.5% Notes (approximately \$451 million). The 8.5% Notes were fully redeemed on January 19, 2012 for approximately \$450 million. In connection with the redemption, we incurred a pre-tax loss from early extinguishment of debt of approximately \$38 million (or \$24 million net of tax). This loss was recorded within discontinued operations in the first quarter of 2012, as that was the period in which the bonds were legally extinguished. The debt extinguishment was completed, in part, using the approximately \$400 million of cash distributed to us from TripAdvisor in connection with the spin-off.



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Our credit ratings are periodically reviewed by rating agencies. In April 2011, in response to our announcement of the TripAdvisor spin-off, Moody's affirmed its Ba1 rating and changed its outlook to from positive to stable, while S&P and Fitch placed the Company's ratings on Credit Watch with negative implications and Rating Watch Negative, respectively. In October 2011, Fitch affirmed its rating at BBB- and removed the rating from Rating Watch Negative, with an outlook of stable. In December 2011, S&P affirmed the Company's BBB- rating and removed the ratings from Credit Watch, with an outlook of stable. Changes in our operating results, cash flows, or financial position could impact the ratings assigned by the various rating agencies. Should our credit ratings be adjusted downward, we may incur higher costs to borrow, which could have a material impact on our financial condition and results of operations.

Under the merchant model, we receive cash from travelers at the time of booking and we record these amounts on our consolidated balance sheets as deferred merchant bookings. We pay our airline suppliers related to these merchant model bookings generally within a few weeks after completing the transaction, but we are liable for the full value of such transactions until the flights are completed. For most other merchant bookings, which is primarily our merchant hotel business, we pay after the travelers' use and subsequent billing from the hotel suppliers. Therefore, generally we receive cash from the traveler prior to paying our suppliers, and this operating cycle represents a working capital source of cash to us. As long as the merchant hotel business grows, we expect that changes in working capital related to merchant hotel transactions will positively impact operating cash flows. However, we continue to evaluate the use of the merchant model versus the agency model in each of our markets. If the merchant hotel model declines relative to our other business models that generally consume working capital such as agency hotel, managed corporate travel or media, or if there are changes to the merchant model or booking patterns which compress the time of receipts of cash from travelers to payment to suppliers, our overall working capital benefits could be reduced, eliminated, or even reversed.

Seasonal fluctuations in our merchant hotel bookings affect the timing of our annual cash flows. During the first half of the year, hotel bookings have traditionally exceeded stays, resulting in much higher cash flow related to working capital. During the second half of the year, this pattern reverses and cash flows are typically negative. While we expect the impact of seasonal fluctuations to continue, merchant hotel growth rates, changes to the model or booking patterns, as well as changes in the relative mix of merchant hotel transactions compared with transactions in our working capital consuming businesses may counteract or intensify the anticipated seasonal fluctuations.

As of March 31, 2012, we had a deficit in our working capital of \$418 million, compared to a deficit of \$279 million as of December 31, 2011. The change in deficit was primarily due to stock repurchases during the first quarter of 2012.

We continue to invest in the development and expansion of our operations. Ongoing investments include but are not limited to improvements to infrastructure, which include our servers, networking equipment and software, release improvements to our software code, platform migrations and consolidation and search engine marketing and optimization efforts. Our future capital requirements may include capital needs for acquisitions, share repurchases, dividend payments or expenditures in support of our business strategy; thus reducing our cash balance and/or increasing our debt. Our capital expenditures for full year 2012 are expected to be slightly above 2011 spending levels.

Our cash flows are as follows:

|                                                                      | Three months ended March 31, |                       | \$ Change |
|----------------------------------------------------------------------|------------------------------|-----------------------|-----------|
|                                                                      | 2012                         | 2011<br>(In millions) |           |
| Cash provided by (used in) continuing operations:                    |                              |                       |           |
| Operating activities                                                 | \$ 848                       | \$ 693                | \$ 155    |
| Investing activities                                                 | (98)                         | (424)                 | 326       |
| Financing activities                                                 | (175)                        | (67)                  | (108)     |
| Net cash provided by (used in) discontinued operations               | (8)                          | 40                    | (48)      |
| Effect of foreign exchange rate changes on cash and cash equivalents | 16                           | 9                     | 7         |

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For the three months ended March 31, 2012, net cash provided by operating activities increased by \$155 million primarily due to increased benefits from working capital changes as well as an increase in operating income.

For the three months ended March 31, 2012, approximately \$326 million less cash was used in investing activities primarily due to decreased net purchases of investments of \$327 million.

We expect to close an acquisition in the second quarter of 2012 for a purchase price not expected to exceed \$215 million.

Cash used in financing activities for the three months ended March 31, 2012 primarily included cash paid to acquire shares of \$198 million, including the repurchased shares under the 2010 authorization discussed below, as well as a \$12 million cash dividend payment, partially offset by \$32 million of proceeds from the exercise of equity awards. Cash used in financing activities for the three months ended March 31, 2011 primarily included cash paid to acquire shares of \$48 million, including the repurchased shares under the 2010 authorization discussed below, as well as a \$19 million cash dividend payment.

In 2010, the Executive Committee, acting on behalf of the Board of Directors, authorized a repurchase of up to 20 million outstanding shares of our common stock. During the three months ended March 31, 2012 and 2011, we repurchased, through open market transactions, 5.8 million and 2.0 million shares (1.0 million on a reverse split adjusted basis) under these authorizations for a total cost of \$192 million and \$41 million, excluding transaction costs. As of April 26, 2012, subsequent to the end of the first quarter of 2012, we repurchased the additional 3 million shares remaining under the 2010 authorization for a total cost of \$99 million, excluding transaction costs.

On April 25, 2012, the Executive Committee, acting on behalf of the Board of Directors, authorized a repurchase of up to 20 million outstanding shares of our common stock. No shares have been repurchased under this authorization as of April 26, 2012 and the authorization has no fixed termination date for the repurchases.

In the first quarter of 2012 and 2011, the Executive Committee, acting on behalf of the Board of Directors, declared and we paid a quarterly cash dividend of \$0.09 and \$0.14 per share of outstanding common stock. In addition, on April 25, 2012, the Executive Committee, acting on behalf of the Board of Directors, declared a quarterly cash dividend of \$0.09 per share of outstanding common stock to stockholders of record as of the close of business on May 30, 2012. Future declarations of dividends are subject to final determination of our Board of Directors.

As of March 31, 2012, there were 30 million privately held warrants outstanding, which if exercised in full, would entitle the holders to acquire 7.4 million common shares of Expedia, Inc. at a weighted average exercise price of \$24.16. All of these warrants expire in May 2012. The holders of the stock warrants may choose at their option, without payment of cash, to reduce the number of shares otherwise obtainable upon exercise for payment (i.e. cashless exercise) in lieu of a cash payment.

In our opinion, available cash, funds from operations and available borrowings will provide sufficient capital resources to meet our foreseeable liquidity needs. There can be no assurance, however, that the cost or availability of future borrowings, including refinancings, if any, will be available on terms acceptable to us.

### ***Contractual Obligations, Commercial Commitments and Off-balance Sheet Arrangements***

There have been no material changes outside the normal course of business to our contractual obligations and commercial commitments since December 31, 2011. Other than our contractual obligations and commercial commitments, we did not have any off-balance sheet arrangements as of March 31, 2012 or December 31, 2011.

### ***Certain Relationships and Related Party Transactions***

For a discussion of certain relationships and related party transactions, including TripAdvisor, see Note 10 Related Party Transactions in the notes to the consolidated financial statements.

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

**Market Risk Management**

There has been no material changes in our market risk during the three months ended March 31, 2012. For additional information, see Item 7A, Quantitative and Qualitative Disclosures About Market Risk, in Part II of our Annual Report on Form 10-K for the year ended December 31, 2011.

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**Part I. Item 4. Controls and Procedures**

***Evaluation of disclosure controls and procedures.***

As required by Rule 13a-15(b) under the Securities Exchange Act of 1934, as amended (the Exchange Act), our management, including our Chairman and Senior Executive, Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e) and 15d-15(e) under the Exchange Act). Based upon that evaluation, our Chairman and Senior Executive, Chief Executive Officer and Chief Financial Officer concluded that, as of the end of the period covered by this report, our disclosure controls and procedures were effective.

***Changes in internal control over financial reporting.***

There were no changes to our internal control over financial reporting that occurred during the quarter ended March 31, 2012 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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### **Part II. Item 1. Legal Proceedings**

In the ordinary course of business, Expedia and its subsidiaries are parties to legal proceedings and claims involving property, personal injury, contract, alleged infringement of third party intellectual property rights and other claims. A discussion of certain legal proceedings can be found in the section titled "Legal Proceedings," of our Annual Report on Form 10-K for the year ended December 31, 2011. The following are developments regarding such legal proceedings:

#### **Litigation Relating to Hotel Occupancy Taxes**

##### ***Actions Filed by Individual States, Cities and Counties***

*Nassau County, New York Litigation.* Defendant online travel companies have filed a motion to dismiss.

*Branson, Missouri Litigation.* On January 28, 2012, the court granted defendants' motion to dismiss holding that online travel companies are not subject to hotel occupancy tax. The city has appealed.

*City of Houston, Texas Litigation.* The city has sought review by the Texas Supreme Court of the decision by the Texas Court of Appeals holding that online travel companies are not subject to hotel occupancy tax.

*Cities of Goodlettsville and Brentwood, Tennessee Litigation.* On February 21, 2012, the court granted the online travel companies' motion for summary judgment and denied the cities' motion for summary judgment, and held that online travel companies are not liable for occupancy taxes.

*City of San Francisco, California Litigation.* The parties have filed cross-motions for summary judgment.

*City of Bowling Green, Kentucky Litigation.* On February 15, 2012, the Kentucky Supreme Court denied the city of Bowling Green's motion for discretionary review of the Court of Appeal's decision that online travel companies are not liable for hotel occupancy tax.

*Village of Rosemont, Illinois Litigation.* The parties have filed cross-motions for summary judgment on damages.

*Lawrence County, Pennsylvania Litigation.* The case has been stayed pending a decision in the city of Philadelphia litigation.

*Pine Bluff, Arkansas Litigation.* On March 30, 2012, the court lifted the stay and the case will proceed.

*Leon County, Florida et. al. Litigation.* On February 3, 2012, plaintiffs filed a motion for summary judgment. On February 8, 2012, the online travel companies filed a motion for summary judgment. On April 19, 2012, the court granted the online travel companies' motion for summary judgment and denied the plaintiffs' motion for summary judgment.

*Leon County v. Expedia, Inc., Florida Department of Revenue Litigation, et al Litigation.* The online travel companies moved to dismiss on grounds similar to those brought by the Florida Department of Revenue in its motion to dismiss brought on December 21, 2011.

*City of Birmingham, Alabama Litigation.* On April 13, 2012, the Alabama Supreme Court affirmed the lower court's grant of summary judgment in favor of the online travel companies and held that hotel occupancy taxes are not due from online travel companies.

*City of Philadelphia Litigation.* On February 2, 2012, the Commonwealth Court of Pennsylvania affirmed the lower court decision and held that hotel occupancy taxes are not due from Expedia. On February 24, 2012, the city filed a petition for review to the Pennsylvania Supreme Court.

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### **Part II. Item 1. Legal Proceedings**

*City of Rome, Georgia Litigation.* The parties have reached a settlement on the issue of payment of future excise taxes under the prior decision by the Georgia Supreme Court.

*McAllister Arkansas Citizen-Taxpayer Litigation.* On February 2, 2012, the court denied the online travel companies' motion to dismiss.

#### ***Notices of Audit or Tax Assessments***

At various times, the Company has also received notices of audit, or tax assessments from municipalities and other taxing jurisdictions concerning our possible obligations with respect to state and local hotel occupancy or related taxes, which are listed in the section titled "Legal Proceedings" of our Annual Report on Form 10-K for the year ended December 31, 2011. In addition, North Carolina has begun or attempted to pursue formal or informal audits or administrative procedures, or stated that they may assert claims against us relating to allegedly unpaid state or local hotel occupancy or related taxes.

The Company believes that the claims discussed above lack merit and will continue to defend vigorously against them.

#### ***Actions Filed by Expedia***

*New York City Litigation.* The City of New York has filed a motion for reargument or leave to appeal.

*Expedia Insurance Litigation.* Expedia has filed a motion for summary judgment.

*Hawaii Tax Court Litigation.* Trial is set for the week of October 15, 2012.

*City of Portland Litigation.* On February 17, 2012, the online travel companies brought suit seeking a declaration that they do not have tax obligations to the city of Portland or Multnomah County. *Expedia, Inc. v. City of Portland*, Case No. 1202-02223 (In the Circuit Court of the State of Oregon for the County of Multnomah). Subsequent to the filing of the suit, the city and county sought to assess and require the online travel companies to pay taxes, interest and penalties. The city/counties' assessments against the Expedia companies total approximately \$21 million, but did not include any supporting detail. On March 22, 2012, the online travel companies successfully brought a motion for a temporary restraining order barring the city and county from proceeding with the tax assessment process and requiring the online travel companies to pay the tax amounts claimed. On March 30, 2012, the city and county filed a motion to dismiss on the basis that the online travel companies should be required to exhaust their administrative remedies including the payment of any taxes allegedly owed before proceeding in a lawsuit.

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**Part II. Item 1A. Risk Factors**

In addition to the other information set forth in this report, you should carefully consider the factors discussed below and in Part I, Item 1A, Risk Factors, in our Annual Report on Form 10-K for the year ended December 31, 2011, which could materially affect our business, financial condition or future results. The risks described below and in our Annual Report on Form 10-K are not the only risks facing the Company. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition and/or operating results.

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### Part II. Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

#### Share Repurchases

In 2010, the Executive Committee, acting on behalf of the Board of Directors, authorized a repurchase of up to 20 million outstanding shares of our common stock.

A summary of the repurchase activity for the first quarter of 2012 is as follows:

| Period              | Total Number<br>of Shares<br>Purchased | Average<br>Price<br>Paid<br>Per<br>Share | Total Number<br>of Shares<br>Purchased<br>as<br>Part of<br>Publicly<br>Announced<br>Plans or<br>Programs | Maximum<br>Number of<br>Shares that<br>May Yet Be<br>Purchased<br>Under Plans<br>or<br>Programs |
|---------------------|----------------------------------------|------------------------------------------|----------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------|
| January 1-31, 2012  |                                        | \$                                       |                                                                                                          | 8,755                                                                                           |
| February 1-29, 2012 | 743                                    | 33.10                                    | 743                                                                                                      | 8,012                                                                                           |
| March 1-31, 2012    | 5,016                                  | 33.44                                    | 5,016                                                                                                    | 2,996                                                                                           |
| Total               | 5,759                                  | \$ 33.39                                 | 5,759                                                                                                    |                                                                                                 |

Subsequent to the end of the first quarter of 2012, we repurchased the additional 3 million shares remaining under the 2010 authorization for a total cost of \$99 million, excluding transaction costs, representing an average repurchase price of \$32.95 per share.

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### **Part II. Item 6. Exhibits**

The exhibits listed below are filed as part of this Quarterly Report on Form 10-Q.

| <b>Exhibit</b> |                                                                                                                                                                                                                                                                                                                                                                                 | <b>Filed</b>    |             | <b>Incorporated by Reference</b> |                |                    |
|----------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------|-------------|----------------------------------|----------------|--------------------|
| <b>No.</b>     | <b>Exhibit Description</b>                                                                                                                                                                                                                                                                                                                                                      | <b>Herewith</b> | <b>Form</b> | <b>SEC File No.</b>              | <b>Exhibit</b> | <b>Filing Date</b> |
| 10.1           | Amended and Restated Employment Agreement between Dhiren R. Fonseca and Expedia, Inc., effective March 30, 2012                                                                                                                                                                                                                                                                 | X               |             |                                  |                |                    |
| 10.2           | Executive Separation and Release of Claims Agreement between Gary M. Fritz and Expedia, Inc., dated as of March 13, 2012                                                                                                                                                                                                                                                        | X               |             |                                  |                |                    |
| 31.1           | Certification of the Chairman and Senior Executive pursuant to Section 302 of the Sarbanes-Oxley Act of 2002                                                                                                                                                                                                                                                                    | X               |             |                                  |                |                    |
| 31.2           | Certification of the Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002                                                                                                                                                                                                                                                                          | X               |             |                                  |                |                    |
| 31.3           | Certification of the Chief Financial Officer pursuant Section 302 of the Sarbanes-Oxley Act of 2002                                                                                                                                                                                                                                                                             | X               |             |                                  |                |                    |
| 32.1           | Certification of the Chairman and Senior Executive pursuant Section 906 of the Sarbanes-Oxley Act of 2002                                                                                                                                                                                                                                                                       | X               |             |                                  |                |                    |
| 32.2           | Certification of the Chief Executive Officer pursuant Section 906 of the Sarbanes-Oxley Act of 2002                                                                                                                                                                                                                                                                             | X               |             |                                  |                |                    |
| 32.3           | Certification of the Chief Financial Officer pursuant Section 906 of the Sarbanes-Oxley Act of 2002                                                                                                                                                                                                                                                                             | X               |             |                                  |                |                    |
| 101*           | The following financial statements from the Company's Quarterly Report on Form 10-Q for the quarter ended March 31, 2012, formatted in XBRL: (i) Consolidated Statements of Operations, (ii) Consolidated Statements of Comprehensive Income (iii) Consolidated Balance Sheets, (iv) Consolidated Statements of Cash Flows, and (v) Notes to Consolidated Financial Statements. |                 |             |                                  |                |                    |

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**Signature**

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 hereunto duly authorized.

April 26, 2012

Expedia, Inc.

By: /s/ MARK D. OKERSTROM  
Mark D. Okerstrom  
Chief Financial Officer

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