

GRAPHIC PACKAGING CORP

Form 10-Q

November 09, 2007

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

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

**For the quarterly period ended September 30, 2007**

**or**

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

**For the transition period from**                    **to**

**COMMISSION FILE NUMBER: 1-13182**

**Graphic Packaging Corporation**

(Exact name of registrant as specified in its charter)

**Delaware**

(State or other jurisdiction of  
incorporation or organization)

**58-2205241**

(I.R.S. employer  
identification no.)

**814 Livingston Court**

**Marietta, Georgia**

(Address of principal executive offices)

**30067**

(Zip Code)

**(770) 644-3000**

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

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

Large accelerated filer  Accelerated filer  Non-accelerated filer

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

Yes  No

As of November 5, 2007, there were 200,978,569 shares of the registrant's Common Stock, par value \$0.01 per share, outstanding.

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***Information Concerning Forward-Looking Statements***

Certain statements regarding the expectations of Graphic Packaging Corporation ( GPC and, together with its subsidiaries, the Company ), including, but not limited to, statements regarding the timing of the proposed combination of the Company s business with that of Alitivity Packaging, LLC, inflationary pressures, cost savings from its continuous improvement programs and manufacturing rationalization, capital spending, depreciation and amortization, interest expense, debt reduction and pension plan contributions in this report constitute forward-looking statements as defined in the Private Securities Litigation Reform Act of 1995. Such statements are based on currently available operating, financial and competitive information and are subject to various risks and uncertainties that could cause actual results to differ materially from the Company s historical experience and its present expectations. These risks and uncertainties include, but are not limited to, inflation of and volatility in raw material and energy costs, the Company s substantial amount of debt, continuing pressure for lower cost products, the Company s ability to implement its business strategies, including productivity initiatives and cost reduction plans, currency movements and other risks of conducting business internationally, and the impact of regulatory and litigation matters, including those that impact the Company s ability to protect and use its intellectual property. Undue reliance should not be placed on such forward-looking statements, as such statements speak only as of the date on which they are made and the Company undertakes no obligation to update such statements. Additional information regarding these and other risks is contained herein in Part II, Item 1A., Risk Factors and in the Company s other filings with the Securities and Exchange Commission.

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**PART I FINANCIAL INFORMATION**  
**ITEM 1. FINANCIAL STATEMENTS**  
**GRAPHIC PACKAGING CORPORATION**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**

<i>In millions, except share and per share amounts</i>	<b>September 30, 2007</b> (Unaudited)	<b>December 31, 2006</b>
<b>ASSETS</b>		
Current Assets:		
Cash and Equivalents	\$ 10.2	\$ 7.1
Receivables, Net	256.9	219.2
Inventories	310.9	287.7
Other Current Assets	25.2	22.9
Assets Held for Sale	35.8	60.8
<b>Total Current Assets</b>	<b>639.0</b>	<b>597.7</b>
Property, Plant and Equipment, Net	1,385.9	1,458.4
Goodwill	642.3	642.3
Intangible Assets, Net	141.8	148.5
Deferred Tax Assets	344.5	344.9
Other Assets	34.2	41.8
<b>Total Assets</b>	<b>\$ 3,187.7</b>	<b>\$ 3,233.6</b>
<b>LIABILITIES</b>		
Current Liabilities:		
Short Term Debt	\$ 18.8	\$ 10.9
Accounts Payable	204.5	203.6
Other Accrued Liabilities	161.8	187.8
Liabilities Held for Sale	27.2	27.7
<b>Total Current Liabilities</b>	<b>412.3</b>	<b>430.0</b>
Long Term Debt	1,930.9	1,910.5
Deferred Tax Liabilities	480.3	465.7
Accrued Pension and Postretirement Benefits	194.0	206.7
Other Noncurrent Liabilities	44.9	39.0
<b>Total Liabilities</b>	<b>3,062.4</b>	<b>3,051.9</b>

**SHAREHOLDERS EQUITY**

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Preferred Stock, par value \$.01 per share; 50,000,000 shares authorized; no shares issued or outstanding

Common Stock, par value \$.01 per share; 500,000,000 shares authorized; 200,978,569 and 200,584,591 shares issued and outstanding at September 30, 2007 and December 31, 2006, respectively

Capital in Excess of Par Value	2.0	2.0
Accumulated Deficit	1,191.0	1,186.8
Accumulated Other Comprehensive Loss	(975.0)	(901.1)
	(92.7)	(106.0)
<b>Total Shareholders Equity</b>	125.3	181.7
<b>Total Liabilities and Shareholders Equity</b>	\$ 3,187.7	\$ 3,233.6

The accompanying notes are an integral part of the Condensed Consolidated Financial Statements.

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**GRAPHIC PACKAGING CORPORATION**  
**CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**  
**(Unaudited)**

	<b>Three Months</b>		<b>Nine Months Ended</b>	
	<b>Ended</b>		<b>September 30,</b>	
	<b>September 30,</b>		<b>September 30,</b>	
<i>In millions, except per share amounts</i>	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
Net Sales	\$612.1	\$595.9	\$1,819.3	\$1,756.0
Cost of Sales	500.1	500.5	1,555.6	1,521.5
Selling, General and Administrative	48.3	48.7	141.5	147.4
Research, Development and Engineering	2.1	2.6	6.7	8.3
Other Expense, Net		1.4	2.1	0.4
Income from Operations	61.6	42.7	113.4	78.4
Interest Income	0.1	0.1	0.3	0.5
Interest Expense	(41.4)	(43.3)	(127.8)	(127.8)
Loss on Early Extinguishment of Debt			(9.5)	
Income (Loss) before Income Taxes and Equity in Net Earnings of Affiliates	20.3	(0.5)	(23.6)	(48.9)
Income Tax Expense	(5.4)	(5.2)	(19.1)	(15.3)
Income (Loss) before Equity in Net Earnings of Affiliates	14.9	(5.7)	(42.7)	(64.2)
Equity in Net Earnings of Affiliates	0.2	0.3	0.7	0.8
Income (Loss) from Continuing Operations	15.1	(5.4)	(42.0)	(63.4)
(Loss) Income from Discontinued Operations, Net of Taxes	(29.0)	0.3	(31.9)	(1.2)
Net Loss	\$ (13.9)	\$ (5.1)	\$ (73.9)	\$ (64.6)
Income (Loss) Per Share Basic				
Continuing Operations	\$ 0.07	\$ (0.03)	\$ (0.21)	\$ (0.31)
Discontinued Operations	(0.14)		(0.16)	(0.01)
Total	\$ (0.07)	\$ (0.03)	\$ (0.37)	\$ (0.32)
Income (Loss) Per Share Diluted				
Continuing Operations	\$ 0.07	\$ (0.03)	\$ (0.21)	\$ (0.31)
Discontinued Operations	(0.14)		(0.16)	(0.01)
Total	\$ (0.07)	\$ (0.03)	\$ (0.37)	\$ (0.32)

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Weighted Average Number of Shares Outstanding	Basic	202.1	200.5	201.7	200.5
Weighted Average Number of Shares Outstanding	Diluted	206.4	200.5	201.7	200.5

The accompanying notes are an integral part of the Condensed Consolidated Financial Statements.

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**GRAPHIC PACKAGING CORPORATION**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**(Unaudited)**

<i>In millions</i>	<b>Nine Months Ended September 30,</b>	
	<b>2007</b>	<b>2006</b>
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Net Loss	\$ (73.9)	\$ (64.6)
Noncash Items Included in Net Loss:		
Depreciation and Amortization	149.7	146.6
Loss on Early Extinguishment of Debt	9.5	
Deferred Income Taxes	14.1	15.0
Pension, Postemployment and Postretirement Benefits Expense, Net of Contributions	(5.2)	(3.0)
Amortization of Deferred Debt Issuance Costs	5.5	6.6
Impairment Charge	25.2	3.9
Other, Net	7.2	1.3
Changes in Operating Assets & Liabilities	(86.7)	(47.6)
Net Cash Provided by Operating Activities	45.4	58.2
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Capital Spending	(61.6)	(63.8)
Other, Net	(3.6)	(0.4)
Net Cash Used in Investing Activities	(65.2)	(64.2)
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Proceeds from Issuance of Debt	1,135.0	
Payment on Debt	(1,140.3)	
Borrowing under Revolving Credit Facilities	681.2	495.8
Payments on Revolving Credit Facilities	(644.0)	(496.8)
Increase in Debt Issuance Costs	(7.0)	
Other, Net	(0.2)	(0.8)
Net Cash Provided by (Used in) Financing Activities	24.7	(1.8)
EFFECT OF EXCHANGE RATE CHANGES ON CASH	0.8	
Net Increase (Decrease) in Cash and Equivalents	5.7	(7.8)
Cash and Equivalents at Beginning of Period (a)	7.3	12.7
Cash and Equivalents at End of Period	13.0	4.9
Less Cash and Equivalents of Assets Held for Sale at End of Period	(2.8)	(0.2)

CASH AND EQUIVALENTS OF CONTINUING OPERATIONS AT END OF PERIOD	\$ 10.2	\$ 4.7
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Note: (a) Does not agree to the Condensed Consolidated Balance Sheet due to cash recorded as assets held for sale.  
The accompanying notes are an integral part of the Condensed Consolidated Financial Statements.

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**GRAPHIC PACKAGING CORPORATION**  
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**(Unaudited)**

**NOTE 1 ORGANIZATION**

Graphic Packaging Corporation ( GPC and, together with its subsidiaries, the Company ) is a leading provider of paperboard packaging solutions for a wide variety of products to multinational and other consumer products companies. The Company strives to provide its customers with packaging solutions designed to deliver marketing and performance benefits at a competitive cost by capitalizing on its low-cost paperboard mills and converting plants, its proprietary carton designs and packaging machines, and its commitment to customer service.

GPC conducts no significant business and has no independent assets or operations other than its ownership of Graphic Packaging International, Inc. GPC fully and unconditionally guarantees substantially all of the debt of Graphic Packaging International, Inc.

The Company s Condensed Consolidated Financial Statements include all subsidiaries in which the Company has the ability to exercise direct or indirect control over operating and financial policies. Intercompany transactions and balances are eliminated in consolidation.

In the Company s opinion, the accompanying financial statements contain all normal recurring adjustments necessary to present fairly the financial position, results of operations and cash flows for the interim periods. The Company s year end Condensed Consolidated Balance Sheet data was derived from audited financial statements. The Company has condensed or omitted certain notes and other information from the interim financial statements presented in this Quarterly Report on Form 10-Q. Therefore, these financial statements should be read in conjunction with the Company s Annual Report on Form 10-K for the year ended December 31, 2006. In addition, the preparation of the Condensed Consolidated Financial Statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the Condensed Consolidated Financial Statements and the reported amounts of revenues and expenses during the reporting period. Actual amounts could differ from those estimates.

The Company has reclassified the presentation of certain prior period information to conform to the current presentation format. As a result, certain assets and liabilities were retrospectively reclassified as held for sale. See Note 12 Discontinued Operations.

**NOTE 2 ACCOUNTING POLICIES**

For a summary of the Company s significant accounting policies, please refer to the Company s Annual Report on Form 10-K for the year ended December 31, 2006.

As described in the Company s significant accounting policies, the preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements. Actual results could differ from these estimates, and changes in these estimates are recorded when known. Certain liabilities of approximately \$3 million were estimated and recorded in connection with the merger of Graphic Packaging International Corporation and Riverwood Holdings, Inc. in 2003 (the 2003 Merger ). In the second quarter of 2007, the Company determined that the liability was no longer required due to the expiration of a condition for which the liability was established. The reversal reduced Selling, General and Administrative expenses by approximately \$3 million in the Condensed Consolidated Statement of Operations.

***Recent Accounting Pronouncements***

In February 2007, the Financial Accounting Standards Board ( FASB ) issued Statement of Financial Accounting Standards ( SFAS ) No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities Including an Amendment of FASB Statement No. 115*, ( SFAS No. 159 ) which is effective for fiscal years beginning after November 15, 2007. This statement permits an entity to choose to measure many financial instruments and certain

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other items at fair value on specified election dates. The Company is currently evaluating the impact of SFAS No. 159.

In July 2006, the FASB issued FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes – an interpretation of FASB Statement 109* ( FIN No. 48 ). FIN No. 48 prescribes a comprehensive model for the financial statement recognition, measurement, presentation and disclosure of uncertain tax positions taken or expected to be taken on an income tax return. FIN No. 48 is effective for fiscal years beginning after December 15, 2006 and the Company adopted FIN 48 effective January 1, 2007. The adoption of FIN No. 48 did not have a material impact on the Company's financial position, results of operations or cash flows.

As of the date of adoption, the Company's liability for unrecognized income tax benefits totaled \$4.1 million, the total of which, if recognized, would affect the annual effective income tax rate. As of September 30, 2007, the Company's unrecognized income tax benefits total \$6.5 million. The increase in unrecognized income tax benefits relates to a judgment received in the Swedish tax court during the first quarter of 2007. The Company intends to defend its tax position but is unable to determine the ultimate outcome of this matter at this time.

The Company files income tax returns in the U.S. federal jurisdiction, and various states and foreign jurisdictions. With few exceptions, the Company is no longer subject to U.S. federal, state and local, or non-U.S. income tax examinations by tax authorities for years before 1999.

The Company recognizes potential accrued interest and penalties related to unrecognized tax benefits within its global operations in income tax expense. Accrued interest and penalties were \$0.8 million and \$1.7 million as of January 1, 2007 and September 30, 2007, respectively.

The Company does not anticipate that total unrecognized tax benefits will significantly change due to the settlement of audits and the expiration of statute of limitations prior to September 30, 2008.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements*, ( SFAS No. 157 ) which defines fair value, establishes guidelines for measuring fair value and expands disclosures regarding fair value measurements. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007. The Company is currently evaluating the impact of SFAS No. 157.

In September 2006, the FASB issued FASB Staff Position AUG AIR-1, *Accounting for Planned Major Maintenance Activities* ( FSP AUG AIR-1 ) which is effective for fiscal years beginning after December 15, 2006. This position statement eliminates the accrue-in-advance method of accounting for planned major maintenance activities. The Company adopted FSP AUG AIR-1 on January 1, 2007 and changed to the direct expensing method allowed by FSP AUG AIR-1 and has retrospectively adjusted its 2006 quarters. The Company's full year 2006 financial statements were not impacted. The adoption of FSP AUG AIR-1 on January 1, 2007 did not have a material impact on the Company's financial position, results of operations or cash flows. As a result of the retrospective adjustment, Cost of Sales, Income from Operations and Net Loss were all negatively impacted by \$1.1 million for the three months ended September 30, 2006 and negatively impacted by \$3.1 million for the nine months ended September 30, 2006.

Additionally, Loss Per Share, both basic and diluted, increased \$0.01 for the three months ended September 30, 2006 and for the nine months ended September 30, 2006.

**NOTE 3 STOCK INCENTIVE PLANS**

The Company has eight equity compensation plans. The Company's only active plan as of September 30, 2007 is the Graphic Packaging Corporation 2004 Stock and Incentive Compensation Plan ( 2004 Plan ), pursuant to which the Company may grant stock options, stock appreciation rights, restricted stock, restricted stock units and other types of stock-based awards to employees and directors of the Company. Stock options and other awards granted under all of the Company's plans generally vest and expire in accordance with terms established at the time of grant.

Effective January 1, 2006, the Company adopted the fair value recognition provisions of FASB Statement No. 123(R), *Share-Based Payment* ( SFAS No. 123R ), using the modified-prospective transition method. The modified-prospective transition method applies to new awards granted, unvested awards as of the date of adoption, and awards modified, repurchased, or cancelled after the date of adoption. Stock-based compensation expense for all

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share-based payment awards granted after January 1, 2006 is based on the grant-date fair value estimated in accordance with the provisions of SFAS No. 123R.

**Stock Options**

The Company has not granted any stock options since 2004. During the nine months ended September 30, 2007, 303,640 stock options were exercised, 560,237 stock options were cancelled and 1,298,010 were settled in cash and cancelled. The total number of shares subject to options at September 30, 2007 was 12,737,514 at a weighted average exercise price of \$7.41.

**Stock Awards, Restricted Stock and Restricted Stock Units**

The Company's 2004 Plan permits the grant of stock awards, restricted stock and restricted stock units (RSUs). All restricted stock and RSUs vest and become unrestricted in one to five years from date of grant. Upon vesting, RSUs granted in 2005, 2006 and 2007 are payable 50% in cash and 50% in shares of common stock. All other RSUs are payable in shares of common stock.

Data concerning RSUs and stock awards granted in the first nine months of 2007 is as follows:

<i>In thousands, except per share amounts</i>	<b>Shares</b>	<b>Weighted Avg. Grant Date Fair Value Per Share</b>
RSUs - Employees	2,501	\$ 4.76
Stock Awards - Board of Directors	50	\$ 4.83

The value of the RSUs is based on the market value of the Company's common stock on the date of grant. The RSUs payable in cash are subject to variable accounting and marked to market accordingly. The RSUs payable in cash are recorded as liabilities, whereas the RSUs payable in shares are recorded in Shareholders' Equity. At September 30, 2007, the Company had 4,799,882 RSUs outstanding. The unrecognized expense at September 30, 2007 is approximately \$9 million and is expected to be recognized over a weighted average period of 1.9 years. The weighted average period does not take into account those RSUs for which vesting and payout will be accelerated upon the consummation of the proposed combination of the Company's business with that of Altivity Packaging, LLC. The value of stock awards is based on the market value of the Company's common stock at the date of grant and recorded in Shareholders' Equity.

During the first nine months of 2007, the Company also issued 16,123 shares of phantom stock, representing compensation deferred by one of its directors. These shares of phantom stock vest on the date of grant and are payable upon termination of service as a director. The Company also has an obligation to issue 189,844 shares in payment of employee deferred compensation.

During the nine months ended September 30, 2007 and 2006, \$6.6 million and \$3.4 million was charged to compensation expense, respectively.

**Table of Contents****NOTE 4 INVENTORIES**

Inventories by major class:

<i>In millions</i>	<b>September 30, 2007</b>	<b>December 31, 2006</b>
Finished goods	\$ 146.0	\$ 150.1
Work in progress	27.8	21.8
Raw materials	85.3	70.9
Supplies	57.7	53.0
	316.8	295.8
Less, Allowance	5.9	8.1
Total	\$ 310.9	\$ 287.7

**NOTE 5 ENVIRONMENTAL AND LEGAL MATTERS*****Environmental Matters***

The Company is subject to a broad range of foreign, federal, state and local environmental, health and safety laws and regulations, including those governing discharges to air, soil and water, the management, treatment and disposal of hazardous substances, solid waste and hazardous wastes, the investigation and remediation of contamination resulting from historical site operations and releases of hazardous substances, and the health and safety of employees.

Compliance initiatives could result in significant costs, which could negatively impact the Company's financial position, results of operations or cash flows. Any failure to comply with such laws and regulations or any permits and authorizations required thereunder could subject the Company to fines, corrective action or other sanctions.

In addition, some of the Company's current and former facilities are the subject of environmental investigations and remediations resulting from historical operations and the release of hazardous substances or other constituents. Some current and former facilities have a history of industrial usage for which investigation and remediation obligations may be imposed in the future or for which indemnification claims may be asserted against the Company. Also, potential future closures or sales of facilities may necessitate further investigation and may result in future remediation at those facilities.

During the first quarter of 2006, the Company self-reported certain violations of its Title V permit under the federal Clean Air Act for its West Monroe, Louisiana mill to the Louisiana Department of Environmental Quality (the LADEQ). The violations relate to the collection, treatment and reporting of hazardous air pollutants. The Company recorded \$0.6 million of expense in the first quarter of 2006 for compliance costs to correct the technical issues causing the Title V permit violations. The Company received a consolidated Compliance Order and notice of potential penalty dated July 5, 2006 from the LADEQ indicating that the Company may be required to pay civil penalties for violations that occurred from 2001 through 2005. Although the Company believes that it is reasonably possible that the LADEQ will assess some penalty, at this time the amount of such penalty is not estimable.

At the request of the County Administrative Board of Östergötland, Sweden, the Company conducted a risk classification of its mill property located in Norrköping, Sweden. Based on the information collected through this activity, the Company determined that some remediation of the site is reasonably probable and recorded a \$3.0 million reserve in the third quarter of 2007. Pursuant to the Sale and Purchase Agreement dated October 16, 2007 between Graphic Packaging International Holding Sweden AB (the Seller) and Lagrummet December nr 1031 Aktiebolg under which the Company's Swedish operations were sold, the Seller retains liability for certain environmental claims after the sale. See Note 13 Subsequent Event regarding the sale of the Swedish operations.

On October 8, 2007, the Company received a notice from the United States Environmental Protection Agency (the EPA) indicating that it is a potentially responsible party for the remedial investigation and feasibility study to be

conducted at the Devil s Swamp Lake site in East Baton Rouge Parish, Louisiana. The Company expects to enter into negotiations with the EPA regarding its potential responsibility and liability, but it is too early in the investigation process to quantify possible costs with respect to such site.

The Company has established reserves for those facilities or issues where liability is probable and the costs are

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reasonably estimable. Except for the Title V permit and Devil's Swamp Lake issues described above, for which it is too early in the investigation and regulatory process to make a determination, the Company believes that the amounts accrued for all of its loss contingencies, and the reasonably possible loss beyond the amounts accrued, are not material to the Company's financial position, results of operations or cash flows. The Company cannot estimate with certainty future corrective compliance, investigation or remediation costs, all of which the Company currently considers to be remote. Costs relating to historical usage or indemnification claims that the Company considers to be reasonably possible are not quantifiable at this time. The Company will continue to monitor environmental issues at each of its facilities and will revise its accruals, estimates and disclosures relating to past, present and future operations, as additional information is obtained.

**Legal Matters**

The Company is a party to a number of lawsuits arising in the ordinary conduct of its business. Although the timing and outcome of these lawsuits cannot be predicted with certainty, the Company does not believe that disposition of these lawsuits will have a material adverse effect on the Company's consolidated financial position, results of operations or cash flows.

**NOTE 6 BUSINESS SEGMENT INFORMATION**

The Company reports its results in two business segments: paperboard packaging and containerboard/other. These segments are evaluated by the chief operating decision maker based primarily on income from operations. The Company's reportable segments are based upon strategic business units that offer different products. The paperboard packaging business segment includes the production and sale of paperboard for its beverage multiple packaging and consumer products packaging businesses from its West Monroe, Louisiana, Macon, Georgia, and Kalamazoo, Michigan mills; carton converting facilities in the United States, Europe, Brazil and Canada; and the design, manufacture and installation of packaging machinery related to the assembly of cartons. The containerboard/other business segment primarily includes the production and sale of linerboard, corrugating medium and kraft paper from paperboard mills in the U.S.

Business segment information is as follows:

<i>In millions</i>	<b>Three Months Ended September 30,</b>		<b>Nine Months Ended September 30,</b>	
	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
<b>NET SALES:</b>				
Paperboard Packaging	\$586.1	\$569.8	\$1,747.0	\$1,685.8
Containerboard/Other	26.0	26.1	72.3	70.2
Total	\$612.1	\$595.9	\$1,819.3	\$1,756.0
<b>INCOME (LOSS) FROM OPERATIONS:</b>				
Paperboard Packaging	\$ 73.8	\$ 51.4	\$ 150.6	\$ 113.5
Containerboard/Other	(3.7)	(3.4)	(10.5)	(13.2)
Corporate	(8.5)	(5.3)	(26.7)	(21.9)
Total	\$ 61.6	\$ 42.7	\$ 113.4	\$ 78.4

**NOTE 7 PENSIONS AND OTHER POSTRETIREMENT BENEFITS**

The Company maintains defined benefit pension plans for its U.S. employees. Benefits are based on years of service and average compensation levels over a period of years. The Company's funding policies with respect to its U.S.



pension plans are to contribute funds to trusts as necessary to at least meet the minimum funding requirements of the U.S. Internal Revenue Code. Plan assets are invested in equities and fixed income securities.

The Company also sponsors three postretirement health care plans that provide medical and life insurance coverage to eligible salaried and hourly retired U.S. employees and their dependents. One of the salaried plans closed to new employees who began employment after December 31, 1993 and the other salaried plan closed to new employees who began after June 15, 1999.

**Table of Contents*****Pension and Postretirement Expense***

The pension and postretirement expenses related to the U.S. plans consisted of the following:

<i>In millions</i>	<b>Pension Benefits</b>				<b>Postretirement Benefits</b>			
	<b>Three Months Ended</b>		<b>Nine Months Ended</b>		<b>Three Months Ended</b>		<b>Nine Months Ended</b>	
	<b>September 30, 2007</b>	<b>2006</b>	<b>September 30, 2007</b>	<b>2006</b>	<b>September 30, 2007</b>	<b>2006</b>	<b>September 30, 2007</b>	<b>2006</b>
Service Cost	\$ 3.4	\$ 4.0	\$ 10.2	\$ 12.0	\$ 0.2	\$0.3	\$ 0.8	\$0.9
Interest Cost	8.8	8.0	26.2	24.2	0.8	0.6	2.0	1.8
Expected Return on Plan Assets	(9.1)	(7.4)	(27.1)	(23.4)				
Amortizations:								
Prior Service Cost	0.8	0.6	2.2	1.6				
Actuarial Loss (Gain)	0.5	1.8	1.7	4.4	(0.1)		(0.1)	
Net Periodic Cost	\$ 4.4	\$ 7.0	\$ 13.2	\$ 18.8	\$ 0.9	\$0.9	\$ 2.7	\$2.7

The Company made contributions of \$21.5 million and \$25.6 million to its U.S. pension plans during the first nine months of 2007 and 2006, respectively. The Company expects to make contributions of approximately \$25 million for the full year 2007. During 2006, the Company made \$25.9 million of contributions to its U.S. pension plans.

The Company made postretirement benefit payments of \$0.9 million and \$2.5 million during the first nine months of 2007 and 2006, respectively. The Company estimates its postretirement benefit payments for the full year 2007 to be approximately \$3 million. During 2006, the Company made postretirement benefit payments of \$2.7 million.

**NOTE 8 DEBT**

On May 16, 2007, the Company entered into a new \$1,355 million Credit Agreement ( *Credit Agreement* ). The Credit Agreement provides for a \$300 million revolving credit facility due on May 16, 2013 and a \$1,055 million term loan facility due on May 16, 2014. The revolving credit facility bears interest at a rate of LIBOR plus 225 basis points and the term loan facility bears interest at a rate of LIBOR plus 200 basis points. The facilities under the Credit Agreement replace the revolving credit facility due on August 8, 2009 and the term loan due on August 8, 2010 under the Company's previous senior secured credit agreement. The Company's obligations under the new Credit Agreement are secured by substantially all of the Company's domestic assets.

In connection with the replacement of the Company's previous revolving credit and term loan facilities and in accordance with Emerging Issues Task Force ( EITF ) 96-19, *Debtor's Accounting for a Modification or Exchange of Debt Instruments* and EITF 98-14, *Debtor's Accounting for Changes in Line-of-Credit or Revolving-Debt Arrangements*, the Company recorded a charge of \$9.5 million, which represented a portion of the unamortized deferred financing costs associated with the previous revolving credit and term loan facilities. This charge is reflected as Loss on Early Extinguishment of Debt in the Company's Condensed Consolidated Statement of Operations. In connection with the new Credit Agreement, the Company recorded approximately \$7 million of deferred financing costs. These costs, combined with the remainder of the deferred financing costs relating to the previous senior secured credit agreement, will be amortized over the term of the new facilities.

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Long-Term Debt consisted of the following:

<i>In millions</i>	<b>September 30, 2007</b>	<b>December 31, 2006</b>
Senior Notes with interest payable semi-annually at 8.5%, payable in 2011	\$ 425.0	\$ 425.0
Senior Subordinated Notes with interest payable semi-annually at 9.5%, payable in 2013	425.0	425.0
Senior Secured Term Loan Facility with interest payable at various dates at floating rates (7.47% at December 31, 2006) payable through 2010		1,055.0
Senior Secured Revolving Facility with interest payable at various dates at floating rates (10.25% at December 31, 2006) payable in 2009		3.6
Senior Secured Term Loan Facility with interest payable at various dates at floating rates (7.45% at September 30, 2007) payable through 2014	1,049.7	
Senior Secured Revolving Facility with interest payable at various dates at floating rates (8.71% at September 30, 2007) payable in 2013	40.0	
Other	1.9	2.1
	1,941.6	1,910.7
Less, current portion	10.7	0.2
Total	\$ 1,930.9	\$ 1,910.5

At September 30, 2007, the Company and its U.S. and international subsidiaries had the following commitments, amounts outstanding and amounts available under revolving credit facilities:

<i>In millions</i>	<b>Total Amount of Commitments</b>	<b>Total Amount Outstanding</b>	<b>Total Amount Available <sup>(a)</sup></b>
Revolving Credit Facility	\$ 300.0	\$ 40.0	\$ 246.0
International Facilities.	21.3	12.5	8.8
Total	\$ 321.3	\$ 52.5	\$ 254.8

Note:

- (a) In accordance with its debt agreements, the Company's availability under its revolving credit facility has been reduced by the amount of standby letters

of credit issued  
of \$14.0 million  
as of  
September 30,  
2007. These  
letters of credit  
are used as  
security against  
its  
self-insurance  
obligations and  
workers  
compensation  
obligations.  
These letters of  
credit expire at  
various dates  
through 2008  
unless extended.

The Credit Agreement and the indentures governing the Senior Notes and Senior Subordinated Notes (the Notes) limit the Company's ability to incur additional indebtedness. Additional covenants contained in the Credit Agreement, among other things, restrict the ability of the Company to dispose of assets, incur guarantee obligations, prepay other indebtedness, make dividend and other restricted payments, create liens, make equity or debt investments, make acquisitions, modify terms of indentures under which the Notes are issued, engage in mergers or consolidations (not including the proposed combination of the Company's business with that of Altiivity Packaging, LLC), change the business conducted by the Company and its subsidiaries, and engage in certain transactions with affiliates. Such restrictions, together with the highly leveraged nature of the Company, could limit the Company's ability to respond to changing market conditions, fund its capital spending program, provide for unexpected capital investments or take advantage of business opportunities.

Under the terms of the Credit Agreement, as long as any commitment remains outstanding under the revolving credit facility, the Company must comply with a maximum consolidated leverage ratio covenant and a minimum consolidated interest expense ratio covenant. The financial covenants contained in the Credit Agreement, among other things, specify the following requirements for each period of four consecutive fiscal quarters ending March, June, September and December of:

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	<b>Maximum Consolidated Debt to Credit Agreement EBITDA Leverage Ratio <sup>(a)</sup></b>	<b>Minimum Credit Agreement EBITDA to Consolidated Interest Expense Ratio <sup>(a)</sup></b>
2007	6.75 to 1.00	1.75 to 1.00
2008	6.00 to 1.00	1.75 to 1.00
2009	5.25 to 1.00	2.00 to 1.00
2010 and thereafter	4.75 to 1.00	2.25 to 1.00

Note:

- (a) Credit Agreement EBITDA is defined in the Credit Agreement as consolidated net income before consolidated net interest expense, non-cash expenses and charges, total income tax expense, depreciation expense, expense associated with amortization of intangibles and other assets, non-cash provisions for reserves for discontinued operations, extraordinary, unusual or non-recurring

gains or losses  
or charges or  
credits, gain or  
loss associated  
with sale or  
write-down of  
assets not in the  
ordinary course  
of business, and  
any income or  
loss accounted  
for by the equity  
method of  
accounting.

At September 30, 2007, the Company was in compliance with the financial covenants in the Credit Agreement and the ratios were as follows:

Consolidated Debt to Credit Agreement EBITDA Leverage Ratio 5.52 to 1.00

Credit Agreement EBITDA to Consolidated Interest Expense Ratio 2.16 to 1.00

The Company's management believes that the presentation of Credit Agreement EBITDA and the related ratios herein provides useful information to investors because borrowings under the Credit Agreement are a key source of the Company's liquidity, and the Company's ability to borrow under the Credit Agreement is dependent on, among other things, its compliance with the financial ratio covenants. Any failure by the Company to comply with these financial ratio covenants could result in an event of default, absent a waiver or amendment from the lenders under such agreement, in which case the lenders may be entitled to declare all amounts owed to be due and payable immediately. The calculations of the components of the Company's financial covenant ratios are listed below:

<i>In millions</i>	<b>Twelve Months Ended September 30, 2007</b>
Net Loss	\$ (109.8)
Income Tax Expense	24.7
Interest Expense, Net	171.8
Loss on Early Extinguishment of Debt	9.5
Depreciation and Amortization	199.1
Dividends Received, Net of Earnings of Equity Affiliates	(0.2)
Pension, Postemployment and Postretirement Benefits Expense	24.2
Merger Related Expenses	1.5
Write-Down of Assets	26.1
RSU Compensation Expense	4.3
Environmental Reserve	3.0
Credit Agreement EBITDA	\$ 354.2
	<b>Twelve Months Ended September 30, 2007</b>
<i>In millions</i>	
Interest Expense, Net	\$ 171.8
Amortization of Deferred Debt Issuance Costs	(7.7)

Consolidated Interest Expense \$ 164.1

<i>In millions</i>	<b>As of September 30, 2007</b>
Short Term Debt	\$ 23.4
Long Term Debt	1,930.9
Total Debt (b)	\$ 1,954.3

Note:

(b) Does not agree to the Condensed Consolidated Balance Sheet due to debt recorded as liabilities held for sale.

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The Company's ability to comply in future periods with the financial covenants in the Credit Agreement, will depend on its ongoing financial and operating performance, which in turn will be subject to economic conditions and to financial, business and other factors, many of which are beyond the Company's control and will be substantially dependent on the selling prices for the Company's products, raw material and energy costs, and the Company's ability to successfully implement its overall business strategies, and meet its profitability objective. If a violation of any of the covenants occurred, the Company would attempt to obtain a waiver or an amendment from its lenders, although no assurance can be given that the Company would be successful in this regard. The Credit Agreement and the indentures governing the Notes have certain cross-default or cross-acceleration provisions; failure to comply with these covenants in any agreement could result in a violation of such agreement which could, in turn, lead to violations of other agreements pursuant to such cross-default or cross-acceleration provisions. If an event of default occurs, the lenders are entitled to declare all amounts owed to be due and payable immediately.

**NOTE 9 COMPREHENSIVE (LOSS) INCOME**

The following table shows the components of Comprehensive (Loss) Income, net of related tax effects:

<i>In millions</i>	<b>Three Months Ended September 30,</b>		<b>Nine Months Ended September 30,</b>	
	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
Net Loss	\$(13.9)	\$ (5.1)	\$(73.9)	\$(64.6)
Other Comprehensive (Loss) Income:				
Derivative Instruments Loss	(4.1)	(7.6)	(0.6)	(15.0)
Currency Translation Adjustments	6.2	(0.5)	9.3	9.5
Amortization of Prior Service Cost	0.8		2.2	
Amortization of Net Actuarial Loss	0.8		2.4	
Comprehensive Loss	\$(10.2)	\$(13.2)	\$(60.6)	\$(70.1)

**NOTE 10 EARNINGS PER SHARE**

The following table summarizes the weighted average number of common shares used in the computation of basic and diluted earnings per share:

<i>In millions</i>	<b>Three Months Ended September 30,</b>		<b>Nine Months Ended September 30,</b>	
	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
Weighted Average Number of Common Shares:				
Basic	202.1	200.5	201.7	200.5
Dilutive effect of Stock Options	0.3			
Dilutive effect of Restricted Stock Units	4.0			
Diluted	206.4	200.5	201.7	200.5

During the three months ended September 30, 2007, 11.9 million options were outstanding but were not included in the computation of diluted earnings per share because the exercise price of the options was greater than the average market price of the common shares.

**NOTE 11 IMPAIRMENT**

In accordance with the FASB SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets* ( SFAS No. 144 ), the Company reviews long-lived assets for impairment when events or changes in circumstances indicate the carrying value of these assets may exceed their current fair values.



During the third quarter of 2007, the Company recognized an impairment charge of \$25.2 million relating to its paperboard mill located in Norrköping, Sweden ( GP-Sweden ). The Company's plan to sell the operations led to the testing for impairment of these long-lived assets. The fair value of the impaired assets was determined based on selling price less cost to sell. The impairment charge is reflected as a component of (Loss) Income from Discontinued Operations on the Condensed Consolidated Statements of Operations. See Note 13 Subsequent Event regarding the sale of the operations.

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During the third quarter of 2006, the Company recognized an impairment charge of \$3.9 million relating to its Sao Paulo, Brazil operations. The continued and projected operating losses and negative cash flows led to the testing for impairment of long-lived assets. The fair value of the impaired assets was determined using the expected present value method and third party appraisals. The impairment charge is reflected as a component of Cost of Sales on the Condensed Consolidated Statements of Operations and as a component of Income from Continuing Operations in the Company's Paperboard Packaging Segment.

**NOTE 12 DISCONTINUED OPERATIONS**

In accordance with SFAS No. 144, the Company classified the long-lived assets of GP-Sweden described in Note 11 Impairment, as held for sale. These long-lived assets comprise operations and cash flows that can be distinguished from the rest of the Company. Since these cash flows will be eliminated from ongoing operations, the results of operations were reported in discontinued operations for all periods presented. See Note 13 Subsequent Event regarding the sale of the operations.

Summarized financial information for discontinued operations is as follows:

<i>In millions</i>	<b>September 30, 2007</b>	<b>December 31, 2006</b>
Cash and Equivalents	\$ 2.8	\$ 0.2
Receivables, Net	13.3	11.7
Inventories	15.8	13.6
Other Current Assets	1.0	1.9
Property, Plant and Equipment, Net		30.3
Other Assets	2.9	3.1
Assets Held for Sale	\$ 35.8	\$ 60.8
Short-Term Debt	\$ 4.6	\$ 1.2
Accounts Payable	11.7	10.8
Other Accrued Liabilities	7.7	6.1
Long-Term Debt		0.2
Deferred Tax Liabilities	3.2	9.4
Liabilities Held for Sale	\$ 27.2	\$ 27.7
Net Assets Held for Sale	\$ 8.6	\$ 33.1

<i>In millions</i>	<b>Three Months Ended September 30,</b>		<b>Nine Months Ended September 30,</b>	
	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
Net Sales	\$ 25.2	\$23.9	\$ 78.1	\$73.4
(Loss) Income before Income Taxes	(35.5)	0.1	(38.5)	(2.5)

GP-Sweden was included in the Paperboard Packaging segment and the Europe geographic area.

**NOTE 13 SUBSEQUENT EVENT**

On October 16, 2007, Graphic Packaging International Holding Sweden AB (the Seller), an indirect wholly-owned subsidiary of the Company, entered into a Sale and Purchase Agreement with Lagrummet December nr 1031 Aktiebolg, a company organized under the laws of Sweden that will be renamed Fiskeby International Holding AB (the Purchaser), and simultaneously completed the transactions contemplated by such agreement. Pursuant to such Purchase and Sales Agreement, the Purchaser acquired all of the outstanding shares of GP-Sweden. GP-Sweden and its subsidiaries are in the business of developing, manufacturing and selling paper and packaging boards made from recycled fiber. The Sale and Purchase Agreement specifies that the purchase price is \$8.6 million and contains customary representations and warranties of the Seller.

The Purchaser is affiliated with Jeffrey H. Coors, the Vice Chairman and a member of the Board of Directors of the

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Company. The Seller undertook the sale of GP-Sweden to the Purchaser after a thorough exploration of strategic alternatives with respect to GP-Sweden. The transactions contemplated by the Sale and Purchase Agreement were approved by the Audit Committee of the Board of Directors of the Company pursuant to its Policy Regarding Related Party Transactions and by the full Board of Directors other than Mr. Coors.

See Note 11-Impairment regarding impairment of GP-Sweden and Note 12-Discontinued Operations regarding discontinued operations of GP-Sweden.

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**ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

**INTRODUCTION**

This management's discussion and analysis of financial conditions and results of operations is intended to provide investors with an understanding of the Company's past performance, its financial condition and its prospects. The following will be discussed and analyzed:

Ø Overview of Business

Ø Overview of 2007 Results

Ø Results of Operations

Ø Financial Condition, Liquidity and Capital Resources

Ø Critical Accounting Policies

Ø New Accounting Standards

Ø Business Outlook

**OVERVIEW OF BUSINESS**

The Company's objective is to strengthen its position as a leading provider of paperboard packaging solutions. To achieve this objective, the Company offers customers its paperboard, cartons and packaging machines, either as an integrated solution or separately. The Company is also implementing strategies (i) to expand market share in its current markets and to identify and penetrate new markets; (ii) to capitalize on the Company's customer relationships, business competencies, and mills and converting assets; (iii) to develop and market innovative products and applications; (iv) and to continue to reduce costs by focusing on operational improvements. The Company's ability to fully implement its strategies and achieve its objective may be influenced by a variety of factors, many of which are beyond its control, such as inflation of raw material and other costs, which the Company cannot always pass through to its customers, and the effect of overcapacity in the worldwide paperboard packaging industry.

**Significant Factors That Impact The Company's Business**

*Substantial Debt Obligations.* The Company has approximately \$1,950 million of outstanding debt obligations as of September 30, 2007. This debt can have significant consequences for the Company, as it requires a significant portion of cash flow from operations to be used for the payment of principal and interest, exposes the Company to the risk of increased interest rates and restricts the Company's ability to obtain additional financing. Covenants in the Company's Credit Agreement limit the Company's ability to incur additional indebtedness, restrict the ability of the Company to dispose of assets, incur guarantee obligations, prepay other indebtedness, make dividend and other restricted payments, create liens, make equity or debt investments, make acquisitions, engage in mergers or consolidations, change the business conducted by the Company and its subsidiaries, and engage in certain transactions with affiliates. These restrictions could limit the Company's flexibility to respond to changing market conditions and competitive pressures. The covenants also require compliance with certain financial ratios. The Company's ability to comply in future periods with the financial covenants will depend on its ongoing financial and operating performance, which in turn will be subject to many other factors, many of which are beyond the Company's control. See *Financial Condition, Liquidity and Capital Resources* *Liquidity and Capital Resources* and *Covenant Restrictions* for additional information regarding the Company's debt obligations.

*Commitment to Cost Reduction.* In light of increasing margin pressure throughout the paperboard packaging industry, the Company has programs in place that are designed to reduce costs, improve productivity and increase profitability. The Company utilizes a global continuous improvement initiative that uses statistical process control to help design and manage many types of activities, including production and maintenance. This includes a Six Sigma process focused on reducing variable and fixed manufacturing and administrative costs. During the first nine months of 2007,

the Company achieved approximately \$34 million in cost savings as compared to the first nine months of 2006, through its continuous improvement programs and other cost reduction initiatives.

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*Impact of Inflation.* The Company's cost of sales consists primarily of energy (including natural gas, fuel oil and electricity), pine pulpwood, hardwood, chemicals, recycled fibers, purchased paperboard, paper, aluminum foil, ink, plastic films and resins, depreciation expense and labor. The Company continues to be negatively impacted by inflationary pressures, which increased costs by \$29.4 million, compared to the first nine months of 2006. The 2007 costs are primarily related to fiber and outside board purchases (\$29.6 million); chemical-based inputs (\$6.9 million); and labor and related benefits (\$1.2 million). These increases were offset by lower energy costs (\$8.0 million), mainly due to the price of natural gas, and other (\$0.3 million). The Company has entered into contracts designed to manage risks associated with future variability in cash flows caused by changes in the price of natural gas. The Company has entered into swaps to hedge approximately 80% and 35% of its expected natural gas usage for the years 2007 and 2008, respectively. The Company believes that inflationary pressures, including higher costs for fiber, wood and chemical-based inputs will continue to negatively impact its results for 2007. Since negotiated sales contracts and the market largely determine the pricing for its products, the Company is at times limited in its ability to raise prices and pass through to its customers all inflationary or other cost increases that the Company may incur, thereby further exacerbating the inflationary problems.

*Market Factors.* As some products can be packaged in different types of materials, the Company's sales are affected by competition from other manufacturers' coated unbleached kraft paperboard, or CUK board, and other substrates' solid bleached sulfate, or SBS, recycled clay coated news, or CCN, and, internationally, white lined chipboard, or WLC. Substitute products also include shrink film, flexible packaging and corrugated containers. In addition, the Company's sales historically are driven by consumer buying habits in the markets its customers serve. New product introductions and promotional activity by the Company's customers and the Company's introduction of new packaging products also impact its sales. The Company's containerboard business is subject to conditions in the cyclical worldwide commodity paperboard markets, which have a significant impact on containerboard sales. In addition, the Company's net sales, income from operations and cash flows from operations are subject to moderate seasonality, with demand usually increasing in the spring and summer due to the seasonality of the worldwide beverage multiple packaging markets. The Company works to maintain market share through efficiency, product innovation and strategic sourcing to its customers; however, pricing and other competitive pressures may occasionally result in the loss of a customer relationship.

**OVERVIEW OF 2007 RESULTS**

This management's discussion and analysis contains an analysis of Net Sales, Income from Operations and other information relevant to an understanding of results of operations. To enhance the understanding of continuing operations, this discussion and analysis excludes discontinued operations for all periods presented. Information on discontinued operations can be found in Note 12 Discontinued Operations in Part I, Item 1, Notes to Condensed Consolidated Financial Statements.

Net Sales in the third quarter of 2007 increased by \$16.2 million, or 2.7%, to \$612.1 million from \$595.9 million in the third quarter of 2006 due primarily to improved pricing across the paperboard packaging segment. Also contributing to the increase was \$5.3 million relating to the favorable foreign currency exchange rates in Europe.

Income from Operations in the third quarter of 2007 increased by \$18.9 million, or 44.3%, to \$61.6 million from \$42.7 million in the third quarter of 2006. The improved pricing and worldwide continuous improvement programs and other cost reduction initiatives were partially offset by higher inflation.

Debt decreased by \$13.3 million during the third quarter of 2007.

On July 9, 2007, the Company entered into a Transaction Agreement and Agreement and Plan of Merger ( Transaction Agreement ) by and among the Company, Bluegrass Container Holdings, LLC ( BCH ), TPG Bluegrass IV, L.P. ( TPG IV ), TPG Bluegrass IV-AIV 2, L.P. ( TPG IV-AIV ), TPG Bluegrass V, L.P. ( TPG V ), TPG Bluegrass V-AIV 2, L.P. ( TPG V-AIV ), Field Holdings, Inc. ( Field Holdings ), TPG FOF V-A, L.P. ( FOF V-A ), TPG FOF V-B, L.P. ( FOF V-B ), BCH Management, LLC (together with Field Holdings, TPG IV, TPG IV-AIV, TPG V, TPG V-AIV, FOF V-A, FOF V-B and any transferee of their





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interests in BCH, the Sellers), New Giant Corporation, a wholly-owned subsidiary of the Company (Newco), and Giant Merger Sub, Inc., a wholly-owned subsidiary of Newco (Merger Sub). The transactions contemplated by such Transaction Agreement are expected to be completed in the fourth quarter of 2007, subject to customary shareholder and regulatory approvals.

The effect of the Transaction is that Newco will hold all of the equity interests of Graphic Packaging Corporation and BCH, which in turn will hold all of the assets of Graphic Packaging International, Inc. and Altivity Packaging, LLC. The Company's current stockholders will initially own approximately 60% of the outstanding common stock of Newco, while the holders of BCH equity interests will initially own approximately 40%.

**RESULTS OF OPERATIONS****Segment Information**

The Company reports its results in two business segments: paperboard packaging and containerboard/other.

<i>In millions</i>	<b>Three Months Ended September 30,</b>		<b>Nine Months Ended September 30,</b>	
	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
<b>NET SALES:</b>				
Paperboard Packaging	\$586.1	\$569.8	\$1,747.0	\$1,685.8
Containerboard/Other	26.0	26.1	72.3	70.2
Total	\$612.1	\$595.9	\$1,819.3	\$1,756.0
<b>INCOME (LOSS) FROM OPERATIONS:</b>				
Paperboard Packaging	\$ 73.8	\$ 51.4	\$ 150.6	\$ 113.5
Containerboard/Other	(3.7)	(3.4)	(10.5)	(13.2)
Corporate	(8.5)	(5.3)	(26.7)	(21.9)
Total	\$ 61.6	\$ 42.7	\$ 113.4	\$ 78.4

**THIRD QUARTER 2007 COMPARED WITH THIRD QUARTER 2006****Net Sales**

<i>In millions</i>	<b>Three Months Ended September 30,</b>			<b>Percent Change</b>
	<b>2007</b>	<b>2006</b>	<b>Increase</b>	
Paperboard Packaging	\$586.1	\$569.8	\$16.3	2.9%
Containerboard/Other	26.0	26.1	(0.1)	(0.4)
Total	\$612.1	\$595.9	\$16.2	2.7%

The components of the change in Net Sales by segment are as follows:

<i>In millions</i>	<b>2006</b>	<b>Three Months Ended September 30, Variances</b>			<b>Total</b>	<b>2007</b>
		<b>Price</b>	<b>Volume/Mix</b>	<b>Exchange</b>		

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Paperboard Packaging	\$569.8	10.3	0.7	5.3	16.3	\$586.1
Containerboard/Other	26.1	(0.3)	0.2		(0.1)	26.0
Total	\$595.9	10.0	0.9	5.3	16.2	\$612.1

**Paperboard Packaging**

The Company's Net Sales from paperboard packaging in the third quarter of 2007 increased due to improved pricing across all product lines as well as favorable foreign currency exchange rates in Europe. The improvement in pricing

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reflects negotiated inflationary cost pass-through and other contractual increases, as well as price increases on open market roll stock. Improved mix for higher value products in North American food and consumer cartons and Europe was offset by lower volume as the Company exited lower margin business. North American beverage carton sales were flat as higher beer sales offset lower soft drink sales.

**Containerboard/Other**

The Company's Net Sales from containerboard/other in the third quarter of 2007 decreased due to lower pricing in the containerboard medium market. Higher volume in the containerboard medium and bag markets was partially offset by lower volume in the liner and post print markets.

**Income (Loss) from Operations**

<i>In millions</i>	<b>Three Months Ended September 30,</b>			
	<b>2007</b>	<b>2006</b>	<b>Increase (Decrease)</b>	<b>Percent Change</b>
Paperboard Packaging	\$73.8	\$51.4	\$22.4	43.6%
Containerboard/Other	(3.7)	(3.4)	(0.3)	(8.8)
Corporate	(8.5)	(5.3)	(3.2)	(60.4)
<b>Total</b>	<b>\$61.6</b>	<b>\$42.7</b>	<b>\$18.9</b>	<b>44.3%</b>

The components of the change in Income (Loss) from Operations by segment are as follows:

<i>In millions</i>	<b>Three Months Ended September 30,</b>							<b>2007</b>
	<b>2006</b>	<b>Price</b>	<b>Volume/Mix</b>	<b>Inflation</b>	<b>Exchange</b>	<b>Other<sup>(a)</sup></b>	<b>Total</b>	
Paperboard Packaging	\$51.4	10.3	2.2	(12.5)	2.5	19.9	22.4	\$73.8
Containerboard/Other	(3.4)	(0.3)					(0.3)	(3.7)
Corporate	(5.3)					(3.2)	(3.2)	(8.5)
<b>Total</b>	<b>\$42.7</b>	<b>10.0</b>	<b>2.2</b>	<b>(12.5)</b>	<b>2.5</b>	<b>16.7</b>	<b>18.9</b>	<b>\$61.6</b>

Note:

(a) Includes the benefits from the Company's cost reduction initiatives as well as the infrastructure upgrade at the Company's West Monroe, LA mill.

**Paperboard Packaging**

The Company's Income from Operations from paperboard packaging in the third quarter of 2007 increased due to the improved pricing, continuing cost reduction initiatives, the improved mix and the favorable impact of foreign currency exchange rates. Performance improved at the Company's West Monroe, LA mill. This reflects increased productivity due to improved machine reliability as well as cost savings. These increases were partially offset by inflationary pressures primarily on fiber and outside board purchases, chemical-based inputs, and labor and related benefits. The third quarter of 2006 was impacted by a \$3.9 million impairment charge related to the Company's Sao Paulo, Brazil operations.

**Containerboard/Other**

The Company's Loss from Operations from containerboard/other in the third quarter of 2007 increased due to the lower pricing in the containerboard medium market.

**Corporate**

The Company's Loss from Operations from corporate in the third quarter of 2007 increased primarily due to higher costs relating to outside consulting services, stock-based compensation awards and management incentives.



**Table of Contents****FIRST NINE MONTHS OF 2007 COMPARED WITH FIRST NINE MONTHS OF 2006****Net Sales**

<i>In millions</i>	Nine Months Ended September 30,			Percent Change
	2007	2006	Increase	
Paperboard Packaging	\$1,747.0	\$1,685.8	\$61.2	3.6%
Containerboard/Other	72.3	70.2	2.1	3.0
Total	\$1,819.3	\$1,756.0	\$63.3	3.6%

The components of the change in Net Sales by segment are as follows:

<i>In millions</i>	Nine Months Ended September 30, Variances					2007
	2006	Price	Volume/Mix	Exchange	Total	
Paperboard Packaging	\$1,685.8	29.8	20.0	11.4	61.2	\$1,747.0
Containerboard/Other	70.2	2.3	(0.2)		2.1	72.3
Total	\$1,756.0	32.1	19.8	11.4	63.3	\$1,819.3

**Paperboard Packaging**

The Company's Net Sales from paperboard packaging in the first nine months of 2007 increased due to improved pricing as well as higher volumes across various product lines. The improvement in pricing reflects negotiated inflationary cost pass-through and other contractual increases, as well as price increases on open market roll stock. The 1.2% increase in volume primarily relates to increased carton sales in the North American food and consumer product markets, as well as sales of open market roll stock in North America. The higher volumes were partially offset by a decline in international beverage market sales. Favorable foreign currency exchange rates in Europe also contributed to the sales increase.

**Containerboard/Other**

The Company's Net Sales from containerboard/other in the first nine months of 2007 increased due to improved pricing in the containerboard medium market, which was partially offset by lower volumes in the containerboard liner, bag and post print markets. The improved pricing represents a year over year increase of approximately \$25 per ton.

**Income (Loss) from Operations**

<i>In millions</i>	Nine Months Ended September 30,			Percent Change
	2007	2006	Increase (Decrease)	
Paperboard Packaging	\$150.6	\$113.5	\$37.1	32.7%
Containerboard/Other	(10.5)	(13.2)	2.7	20.5
Corporate	(26.7)	(21.9)	(4.8)	(21.9)
Total	\$113.4	\$78.4	\$35.0	44.6%

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The components of the change in Income (Loss) from Operations by segment are as follows:

<i>In millions</i>	Nine Months Ended September 30,						Total	2007
	2006	Price	Volume/Mix	Inflation	Exchange	Other <sup>(a)</sup>		
Paperboard Packaging	\$ 113.5	29.8	4.4	(28.4)	5.8	25.5	37.1	\$ 150.6
Containerboard/Other	(13.2)	2.3	1.4	(1.0)			2.7	(10.5)
Corporate	(21.9)					(4.8)	(4.8)	(26.7)
Total	\$ 78.4	32.1	5.8	(29.4)	5.8	20.7	35.0	\$ 113.4

Note:

- (a) Includes the benefits from the Company's cost reduction initiatives and the impact of higher depreciation and amortization expense as well as the infrastructure upgrade at the Company's West Monroe, LA mill.

**Paperboard Packaging**

The Company's Income from Operations from paperboard packaging in the first nine months of 2007 increased due to the improved pricing, cost reduction initiatives, the higher volumes and the favorable impact of foreign currency exchange rates. These increases were partially offset by inflationary pressures primarily on fiber and outside board purchases, chemical-based inputs, labor and related benefits and higher depreciation and amortization. Although the West Monroe, LA mill experienced improved performance in the third quarter of 2007, the first nine months of 2007 was unfavorably impacted by continued infrastructure upgrades and expenses related to a planned maintenance outage. Higher expenses in Europe, primarily relating to start up costs for a new converting facility in France unfavorably impacted the quarter. 2006 was unfavorably impacted by higher manufacturing expenses primarily related to an unexpected failure in a major turbine generator and to upgrade the Company's maintenance program at the West Monroe, LA mill. The first nine months of 2006 was also impacted by a \$3.9 million impairment charge related to the Company's Sao Paulo, Brazil operations.

**Containerboard/Other**

Company's Loss from Operations from containerboard/other in the first nine months of 2007 decreased due primarily to the improved pricing in the containerboard medium market and improved product mix resulting from lower containerboard bag sales which are sold at lower margins, partially offset by higher inflation.

**Corporate**

The Company's Loss from Operations from corporate in the first nine months of 2007 increased due to higher costs relating to stock-based compensation awards, management incentives and outside consulting services. Partially

offsetting these increases was the reversal of a \$3.0 million liability recorded at the time of the 2003 Merger. For more information, see [Critical Accounting Policies](#) in this section. In addition, 2006 included a favorable legal settlement.

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**INTEREST INCOME, INTEREST EXPENSE, INCOME TAX EXPENSE AND EQUITY IN NET EARNINGS OF AFFILIATES**

**Interest Income**

Interest Income decreased to \$0.3 million in the first nine months of 2007 from \$0.5 million in the first nine months of 2006 primarily due to lower average cash balances.

**Interest Expense**

Interest Expense was \$127.8 million in the first nine months of 2007 and 2006. Interest Expense increased due to higher interest rates on the unhedged portion of the Company's floating rate debt. This increase was offset by lower average debt balances during the first nine months of 2007 and the refinancing of the Credit Agreement in May 2007. As of September 30, 2007, approximately 35% of the Company's total debt was subject to floating interest rates.

**Loss on Early Extinguishment of Debt**

Loss on Early Extinguishment of Debt was \$9.5 million in the first nine months of 2007. For more information see Liquidity and Capital Resources in this section.

**Income Tax Expense**

During the first nine months of 2007, the Company recognized Income Tax Expense of \$19.1 million on Loss before Income Taxes and Equity in Net Earnings of Affiliates of \$23.6 million. During the first nine months of 2006, the Company recognized Income Tax Expense of \$15.3 million on Loss before Income Taxes and Equity in Net Earnings of Affiliates of \$48.9 million. Income Tax Expense for the first nine months of 2007 and 2006 was primarily due to the noncash expense of \$14.6 million associated with the amortization of goodwill for tax purposes and for 2007, an increase in a liability related to a judgment received in a Swedish tax court.

**Equity in Net Earnings of Affiliates**

Equity in Net Earnings of Affiliates was \$0.7 million the first nine months of 2007 and \$0.8 million in the first nine months of 2006 and is related to the Company's equity investment in the joint venture Rengo Riverwood Packaging, Ltd.

**DISCONTINUED OPERATIONS**

On October 16, 2007, Graphic Packaging International Holding Sweden AB (the Seller), an indirect wholly-owned subsidiary of the Company, entered into a Sale and Purchase Agreement with Lagrummet December nr 1031 Aktiebolg, a company organized under the laws of Sweden that will be renamed Fiskeby International Holding AB (the Purchaser), and simultaneously completed the transactions contemplated by such agreement. Pursuant to such Purchase and Sales Agreement, the Purchaser will acquire all of the outstanding shares of Graphic Packaging International Sweden (GP-Sweden). GP-Sweden and its subsidiaries are in the business of developing, manufacturing and selling paper and packaging boards made from recycled fiber. The Sale and Purchase Agreement specifies that the purchase price is \$8.6 million and contains customary representations and warranties of the Seller.

The Purchaser is affiliated with Jeffrey H. Coors, the Vice Chairman and a member of the Board of Directors of the Company. The Seller undertook the sale of GP-Sweden to the Purchaser after a thorough exploration of strategic alternatives with respect to GP-Sweden. The transactions contemplated by the Sale and Purchase Agreement were approved by the Audit Committee of the Board of Directors of the Company pursuant to its Policy Regarding Related Party Transactions and by the full Board of Directors other than Mr. Coors.

In accordance with the FASB SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets* (SFAS No. 144), the Company reviews long-lived assets for impairment when events or changes in circumstances indicate the carrying value of these assets may exceed their current fair values. During the third quarter of 2007, the



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Company recognized an impairment charge of \$25.2 million relating to GP-Sweden. The Company's plan to sell the operations led to the testing for impairment of long-lived assets. The fair value of the impaired assets was determined based on selling price less cost to sell. The impairment charge is reflected as a component of (Loss) Income from Discontinued Operations on the Condensed Consolidated Statements of Operations.

In accordance with SFAS No. 144, the financial results of this business are classified as a discontinued operation for all periods presented in the accompanying Condensed Consolidated Financial Statements.

See Note 11 Impairment and Note 12 Discontinued Operations in Part I, Item 1, Notes to Condensed Consolidated Financial Statements.

**Table of Contents****FINANCIAL CONDITION, LIQUIDITY AND CAPITAL RESOURCES**

The Company broadly defines liquidity as its ability to generate sufficient funds from both internal and external sources to meet its obligations and commitments. In addition, liquidity includes the ability to obtain appropriate debt and equity financing and to convert into cash those assets that are no longer required to meet existing strategic and financial objectives. Therefore, liquidity cannot be considered separately from capital resources that consist of current or potentially available funds for use in achieving long-range business objectives and meeting debt service commitments.

**Cash Flows**

Cash and Equivalents increased by \$5.7 million in the first nine months of 2007. Cash provided by operating activities in the first nine months of 2007 totaled \$45.4 million, compared to \$58.2 million in 2006. This decrease was principally due to the timing of interest payments as a result of the refinancing of the Company's previous senior credit agreement on May 16, 2007. Additionally, the higher net loss was partially offset by the non-cash add back for the impairment charge and the loss on early extinguishment of debt. Changes in Operating Assets & Liabilities used \$86.7 million primarily from an increase in Receivables, an increase in Inventories, and a decrease in Accrued Liabilities. Cash used in investing activities in the first nine months of 2007 totaled \$65.2 million, compared to \$64.2 million in 2006. Cash provided by financing activities in the first nine months in 2007 totaled \$24.7 million, compared to \$1.8 million used in 2006. This increase was due to higher net borrowings under the Company's revolving credit facilities. Depreciation and amortization during the first nine months of 2007 totaled \$149.7 million.

**Liquidity and Capital Resources**

The Company's liquidity needs arise primarily from debt service on its substantial indebtedness and from the funding of its capital expenditures, ongoing operating costs and working capital. The Company believes that cash generated from operations, together with the amounts available under the revolving credit facility will be adequate to meet its debt service, capital expenditures, ongoing operating costs and working capital needs.

On May 16, 2007, the Company entered into a new \$1,355 million Credit Agreement ( "Credit Agreement" ). The Credit Agreement provides for a \$300 million revolving credit facility due on May 16, 2013 and a \$1,055 million term loan facility due on May 16, 2014. The revolving credit facility bears interest at a rate of LIBOR plus 225 basis points and the term loan facility bears interest at a rate of LIBOR plus 200 basis points. The facilities under the Credit Agreement replace the revolving credit facility due on August 8, 2009 and the term loan due on August 8, 2010 under the Company's previous senior secured credit agreement. The Company's obligations under the new Credit Agreement are secured by substantially all of the Company's domestic assets.

In connection with the replacement of the Company's previous revolving credit and term loan facilities and in accordance with Emerging Issues Task Force ( EITF ) 96-19, *Debtor's Accounting for a Modification or Exchange of Debt Instruments* and EITF 98-14, *Debtor's Accounting for Changes in Line-of-Credit or Revolving-Debt Arrangements* , the Company recorded a charge of \$9.5 million, which represented a portion of the unamortized deferred financing costs associated with the previous revolving credit and term loan facilities. This charge is reflected as Loss on Early Extinguishment of Debt in the Company's Condensed Consolidated Statement of Operations. In connection with the new Credit Agreement, the Company recorded approximately \$7 million of deferred financing costs. These costs, combined with the remainder of the deferred financing costs relating to the previous senior secured credit agreement, will be amortized over the term of the new facilities.

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Long-Term Debt consisted of the following:

<i>In millions</i>	<b>September 30, 2007</b>	<b>December 31, 2006</b>
Senior Notes with interest payable semi-annually at 8.5%, payable in 2011	\$ 425.0	\$ 425.0
Senior Subordinated Notes with interest payable semi-annually at 9.5%, payable in 2013	425.0	425.0
Senior Secured Term Loan Facility with interest payable at various dates at floating rates (7.47% at December 31, 2006) payable through 2010		1,055.0
Senior Secured Revolving Facility with interest payable at various dates at floating rates (10.25% at December 31, 2006) payable in 2009		3.6
Senior Secured Term Loan Facility with interest payable at various dates at floating rates (7.45% at September 30, 2007) payable through 2014	1,049.7	
Senior Secured Revolving Facility with interest payable at various dates at floating rates (8.71% at September 30, 2007) payable in 2013	40.0	
Other	1.9	2.1
	1,941.6	1,910.7
Less, current portion	10.7	0.2
Total	\$ 1,930.9	\$ 1,910.5

At September 30, 2007, the Company and its U.S. and international subsidiaries had the following commitments, amounts outstanding and amounts available under revolving credit facilities:

<i>In millions</i>	<b>Total Amount of Commitments</b>	<b>Total Amount Outstanding</b>	<b>Total Amount Available <sup>(a)</sup></b>
Revolving Credit Facility	\$ 300.0	\$ 40.0	\$ 246.0
International Facilities	21.3	12.5	8.8
Total	\$ 321.3	\$ 52.5	\$ 254.8

Note:

- (a) In accordance with its debt agreements, the Company's availability under its revolving credit facility has been reduced by the amount of standby letters

of credit issued  
of \$14 million  
as of  
September 30,  
2007. These  
letters of credit  
are used as  
security against  
its  
self-insurance  
obligations and  
workers  
compensation  
obligations.  
These letters of  
credit expire at  
various dates  
through 2008  
unless extended.

Principal and interest payments under the term loan facility and the revolving credit facility, together with principal and interest payments on the Senior Notes and the Senior Subordinated Notes, represent significant liquidity requirements for the Company. Based upon current levels of operations, anticipated cost-savings and expectations as to future growth, the Company believes that cash generated from operations, together with amounts available under its revolving credit facility and other available financing sources, will be adequate to permit the Company to meet its debt service obligations, necessary capital expenditure program requirements, ongoing operating costs and working capital needs, although no assurance can be given in this regard. The Company's future financial and operating performance, ability to service or refinance its debt and ability to comply with the covenants and restrictions contained in its debt agreements (see "Covenant Restrictions"), will be subject to future economic conditions and to financial, business and other factors, many of which are beyond the Company's control and will be substantially dependent on the selling prices and demand for the Company's products, raw material and energy costs, and the Company's ability to successfully implement its overall business and profitability strategies.

Effective as of September 30, 2007, the Company had approximately \$1.4 billion of net operating loss carryforwards (NOLs) for U.S. federal income tax purposes. These NOLs generally may be used by the Company to offset taxable income earned in subsequent taxable years.

#### **Covenant Restrictions**

The Credit Agreement and the indentures governing the Senior Notes and Senior Subordinated Notes (the Notes) limit the Company's ability to incur additional indebtedness. Additional covenants contained in the Credit Agreement, among other things, restrict the ability of the Company to dispose of assets, incur guarantee obligations, prepay other indebtedness, make dividend and other restricted payments, create liens, make equity or debt investments, make acquisitions, modify terms of indentures under which the Notes are issued, engage in mergers or consolidations (not including the proposed combination of the Company's business with that of Altiivity Packaging,

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LLC), change the business conducted by the Company and its subsidiaries, and engage in certain transactions with affiliates. Such restrictions, together with the highly leveraged nature of the Company, could limit the Company's ability to respond to changing market conditions, fund its capital spending program, provide for unexpected capital investments or take advantage of business opportunities.

Under the terms of the Credit Agreement, as long as any commitment remains outstanding under the revolving credit facility, the Company must comply with a maximum consolidated leverage ratio covenant and a minimum consolidated interest expense ratio covenant. The financial covenants contained in the Credit Agreement, among other things, specify the following requirements for each period of four consecutive fiscal quarters ending March, June, September and December of:

	<b>Maximum Consolidated Debt to Credit Agreement EBITDA Leverage Ratio <sup>(a)</sup></b>	<b>Minimum Credit Agreement EBITDA to Consolidated Interest Expense Ratio <sup>(a)</sup></b>
2007	6.75 to 1.00	1.75 to 1.00
2008	6.00 to 1.00	1.75 to 1.00
2009	5.25 to 1.00	2.00 to 1.00
2010 and thereafter	4.75 to 1.00	2.25 to 1.00

Note:

(a) Credit Agreement EBITDA is defined in the Credit Agreement as consolidated net income before consolidated net interest expense, non-cash expenses and charges, total income tax expense, depreciation expense, expense associated with amortization of intangibles and other assets, non-cash provisions for

reserves for discontinued operations, extraordinary, unusual or non-recurring gains or losses or charges or credits, gain or loss associated with sale or write-down of assets not in the ordinary course of business, and any income or loss accounted for by the equity method of accounting.

At September 30, 2007, the Company was in compliance with the financial covenants in the Credit Agreement and the ratios were as follows:

Consolidated Debt to Credit Agreement EBITDA Leverage Ratio 5.52 to 1.00

Credit Agreement EBITDA to Consolidated Interest Expense Ratio 2.16 to 1.00

The Company's management believes that the presentation of Credit Agreement EBITDA and the related ratios herein provides useful information to investors because borrowings under the Credit Agreement are a key source of the Company's liquidity, and the Company's ability to borrow under the Credit Agreement is dependent on, among other things, its compliance with the financial ratio covenants. Any failure by the Company to comply with these financial ratio covenants could result in an event of default, absent a waiver or amendment from the lenders under such agreement, in which case the lenders may be entitled to declare all amounts owed to be due and payable immediately.

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The calculations of the components of the Company's financial covenant ratios are listed below:

<i>In millions</i>	<b>Twelve Months Ended September 30, 2007</b>
Net Loss	\$ (109.8)
Income Tax Expense	24.7
Interest Expense, Net	171.8
Loss on Early Extinguishment of Debt	9.5
Depreciation and Amortization	199.1
Dividends Received, Net of Earnings of Equity Affiliates	(0.2)
Pension, Postemployment and Postretirement Benefits Expense	24.2
Merger Related Expenses	1.5
Write-Down of Assets	26.1
RSU Compensation Expense	4.3
Environmental Reserve	3.0
Credit Agreement EBITDA	\$ 354.2

<i>In millions</i>	<b>Twelve Months Ended September 30, 2007</b>
Interest Expense, Net	\$ 171.8
Amortization of Deferred Debt Issuance Costs	(7.7)
Consolidated Interest Expense	\$ 164.1

<i>In millions</i>	<b>As of September 30, 2007</b>
Short Term Debt	\$ 23.4
Long Term Debt	1,930.9
Total Debt(a)	\$ 1,954.3

Note:

(a) Does not agree to the Condensed Consolidated Balance Sheet due to debt recorded as liabilities held for sale. The Company's ability to comply in future periods with the financial covenants in the Credit Agreement, will depend on its ongoing financial and operating performance, which in turn will be subject to economic conditions and to financial, business and other factors, many of which are beyond the Company's control and will be substantially dependent on the selling prices for the Company's products, raw material and energy costs, and the Company's ability to successfully implement its overall business strategies, and meet its profitability objective. If a violation of any of the covenants occurred, the Company would attempt to obtain a waiver or an amendment from its lenders, although no assurance can be given that the Company would be successful in this regard. The Credit Agreement and the indentures

governing the Notes have certain cross-default or cross-acceleration provisions; failure to comply with these covenants in any agreement could result in a violation of such agreement which could, in turn, lead to violations of other agreements pursuant to such cross-default or cross-acceleration provisions. If an event of default occurs, the lenders are entitled to declare all amounts owed to be due and payable immediately.

**Capital Investment**

The Company's capital investment in the first nine months of 2007 was \$61.6 million, compared to \$63.8 million in the first nine months of 2006. During the first nine months of 2007, the Company had capital spending of \$33.2 million for improving process capabilities, \$18.7 million for capital spares, \$9.5 million for manufacturing packaging machinery and \$0.2 million for compliance with environmental laws and regulations.

**Environmental Matters**

The Company is subject to a broad range of foreign, federal, state and local environmental, health and safety laws and regulations, including those governing discharges to air, soil and water, the management, treatment and disposal of hazardous substances, solid waste and hazardous wastes, the investigation and remediation of contamination resulting from historical site operations and releases of hazardous substances, and the health and safety of employees.

Compliance initiatives could result in significant costs, which could negatively impact the Company's financial position, results of operations or cash flows. Any failure to comply with such laws and regulations or any permits and authorizations required thereunder could subject the Company to fines, corrective action or other sanctions.



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In addition, some of the Company's current and former facilities are the subject of environmental investigations and remediations resulting from historical operations and the release of hazardous substances or other constituents. Some current and former facilities have a history of industrial usage for which investigation and remediation obligations may be imposed in the future or for which indemnification claims may be asserted against the Company. Also, potential future closures or sales of facilities may necessitate further investigation and may result in future remediation at those facilities.

During the first quarter of 2006, the Company self-reported certain violations of its Title V permit under the federal Clean Air Act for its West Monroe, Louisiana mill to the LADEQ. The violations relate to the collection, treatment and reporting of hazardous air pollutants. The Company recorded \$0.6 million of expense in 2006 for compliance costs to correct the technical issues causing the Title V permit violations. In addition, the Company may be required to pay civil penalties for violations that occurred from 2001 through 2005. Although the Company believes that it is reasonably possible that the LADEQ will assess some penalty, at this time the amount of such penalty is not estimable.

At the request of the County Administrative Board of Östergötland, Sweden, the Company conducted a risk classification of its mill property located in Norrköping, Sweden. Based on the information collected through this activity, the Company determined that some remediation of the site is reasonably probable and recorded a \$3.0 million reserve in the third quarter of 2007. Pursuant to the Sale and Purchase Agreement dated October 16, 2007 between Graphic Packaging International Holding Sweden AB (the Seller) and Lagrummet December nr 1031 Aktiebolg under which the Company's Swedish operations were sold, the Seller retains liability for certain environmental claims after the sale. See Note 13 Subsequent Event regarding the sale of the Swedish operations.

On October 8, 2007, the Company received a notice from the United States Environmental Protection Agency (the EPA) indicating that it is a potentially responsible party for the remedial investigation and feasibility study to be conducted at the Devil's Swamp Lake site in East Baton Rouge Parish, Louisiana. The Company expects to enter into negotiations with the EPA regarding its potential responsibility and liability, but it is too early in the investigation process to quantify possible costs with respect to such site.

The Company has established reserves for those facilities or issues where liability is probable and the costs are reasonably estimable. Except for the Title V permit and Devil's Swamp Lake issues described above, for which it is too early in the investigation and regulatory process to make a determination, the Company believes that the amounts accrued for all of its loss contingencies, and the reasonably possible loss beyond the amounts accrued, are not material to the Company's financial position, results of operations or cash flows. The Company cannot estimate with certainty future corrective compliance, investigation or remediation costs, all of which the Company currently considers to be remote. Costs relating to historical usage or indemnification claims that the Company considers to be reasonably possible are not quantifiable at this time. The Company will continue to monitor environmental issues at each of its facilities and will revise its accruals, estimates and disclosures relating to past, present and future operations as additional information is obtained.

**CRITICAL ACCOUNTING POLICIES**

The preparation of financial statements in conformity with United States generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of net sales and expenses during the reporting period. Actual results could differ from these estimates, and changes in these estimates are recorded when known. The critical accounting policies used by management in the preparation of the Company's consolidated financial statements are those that are important both to the presentation of the Company's financial condition and results of operations and require significant judgments by management with regard to estimates used.

Certain liabilities of approximately \$3 million were estimated and recorded in connection with the 2003 Merger. In the second quarter of 2007, the Company determined that the liability was no longer required due to the expiration of a condition for which the liability was established. The reversal reduced Selling, General and Administrative expenses by approximately \$3 million on the Condensed Consolidated Statement of Operations.

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The Company's most critical accounting policies which require significant judgment or involve complex estimations are described in the Company's Annual Report on Form 10-K for the year ended December 31, 2006.

**NEW ACCOUNTING STANDARDS**

For a discussion of recent accounting pronouncements impacting the Company, see Note 2 in Part I, Item 1, Notes to Condensed Consolidated Financial Statements.

**BUSINESS OUTLOOK**

The Company expects inflationary pressures for production inputs, including higher costs for fiber, wood and chemical-based inputs, to continue to impact results in 2007. These increases should be somewhat offset by lower energy costs.

To help offset inflation in 2007, the Company expects to realize approximately \$40 million to \$50 million in year over year operating cost savings from its continuous improvement programs.

Total capital investment for 2007 is expected to be between approximately \$100 million and \$110 million and is expected to relate principally to improving the Company's process capabilities, including manufacturing cost reductions, the production of packaging machinery, the acquisition of capital spares and compliance with environmental laws and regulations.

The Company also expects the following in 2007:

Depreciation and amortization, excluding discontinued operations, between \$190 million and \$200 million.

Interest expense of \$160 million to \$170 million, including approximately \$8 million of non-cash interest expense associated with amortization of debt issuance costs.

Debt reduction of approximately \$60 million.

Pension plan contributions of \$25 million to \$30 million.

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**ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK**

For a discussion of certain market risks related to the Company, see Part II, Item 7A, Quantitative and Qualitative Disclosure about Market Risk, in the Company's Annual Report on Form 10-K for the year ended December 31, 2006. There have been no significant developments with respect to derivatives or exposure to market risk during the first nine months of 2007; for a discussion of the Company's Financial Instruments, Derivatives and Hedging Activities, see Note 11 in Notes to Consolidated Financial Statements in the Company's Annual Report on Form 10-K for the year ended December 31, 2006 and Management's Discussion and Analysis of Financial Condition and Results of Operations - Financial Condition, Liquidity and Capital Resources.

**ITEM 4. CONTROLS AND PROCEDURES**

*Disclosure Controls and Procedures*

The Company's management has carried out an evaluation, with the participation of its Chief Executive Officer and Chief Financial Officer, of the effectiveness of the Company's disclosure controls and procedures pursuant to Rule 13a-15 of the Securities Exchange Act of 1934, as amended. Based upon such evaluation, management has concluded that the Company's disclosure controls and procedures were effective as of September 30, 2007.

*Changes in Internal Control over Financial Reporting*

There was no change in the Company's internal control over financial reporting that occurred during the fiscal quarter ended September 30, 2007 that has materially affected, or is likely to materially affect, the Company's internal control over financial reporting.

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**PART II OTHER INFORMATION**

**ITEM 1. LEGAL PROCEEDINGS**

The Company is a party to a number of lawsuits arising in the ordinary conduct of its business. Although the timing and outcome of these lawsuits cannot be predicted with certainty, the Company does not believe that disposition of these lawsuits will have a material adverse effect on the Company's consolidated financial position, results of operations or cash flows. For more information see Management's Discussion and Analysis of Financial Condition and Results of Operations Environmental Matters.

**ITEM 1A. RISK FACTORS**

There have been no material changes from the risk factors previously disclosed in our Form 10-K for the year ended December 31, 2006.

**ITEM 6. EXHIBITS**

a) Exhibit Index

<b>Exhibit Number</b>	<b>Description</b>
31.1	Certification required by Rule 13a-14(a).
31.2	Certification required by Rule 13a-14(a).
32.1	Certification required by Section 1350 of Chapter 63 of Title 18 of the United States Code.
32.2	Certification required by Section 1350 of Chapter 63 of Title 18 of the United States Code.

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**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

**GRAPHIC PACKAGING CORPORATION**

(Registrant)

/s/ STEPHEN A. HELLRUNG Stephen A. Hellrung	Senior Vice President, General Counsel and Secretary	November 9, 2007
/s/ DANIEL J. BLOUNT Daniel J. Blount	Senior Vice President and Chief Financial Officer (Principal Financial Officer)	November 9, 2007
/s/ DEBORAH R. FRANK Deborah R. Frank	Vice President and Controller (Principal Accounting Officer)	November 9, 2007