

SCHWEITZER MAUDUIT INTERNATIONAL INC  
Form 10-K  
February 24, 2012  
UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 10-K

(Mark One)

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

For the year ended December 31, 2011

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

1-13948

(Commission file number)

SCHWEITZER-MAUDUIT INTERNATIONAL, INC.  
(Exact name of registrant as specified in its charter)

Delaware  
(State or other jurisdiction of incorporation or organization)

62-1612879  
(I.R.S. Employer Identification No.)

100 North Point Center East, Suite 600  
Alpharetta, Georgia  
(Address of principal executive offices)

30022  
(Zip code)

1-800-514-0186  
(Registrant's telephone number, including area code)

Title of each class  
Common stock, par value \$0.10 per share

Name of exchange on which registered  
New York Stock Exchange, Inc.

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined by Rule 405 of the Securities Act.  
Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes  No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

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

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

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

The aggregate market value of the outstanding common stock, par value \$0.10 per share (the “Common Stock”), held by non-affiliates of the registrant as of June 30, 2011 (the last business day of the registrant's most recently completed second fiscal quarter) was \$895.4 million, based on the last sale price for the Common Stock of \$56.15 per share as reported on the New York Stock Exchange on said date. For purposes of the foregoing sentence only, all directors and executive officers are assumed to be affiliates.

There were 15,953,378 shares of Common Stock issued and outstanding as of February 22, 2012.

#### DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant's definitive Proxy Statement relating to its 2012 Annual Meeting of Stockholders scheduled to be held on April 26, 2012 (“the 2012 Proxy Statement”) and filed pursuant to Regulation 14A are incorporated by reference into Part III of this Form 10-K.

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PART I

Item 1. Business

GENERAL

Schweitzer-Mauduit International, Inc. (referred to, with its consolidated subsidiaries, as “we”, “us”, “our”, the “Company”, “SWM INTL” or “SWM” unless the context indicates otherwise) is a multinational diversified producer of premium specialty papers headquartered in the United States of America. We manufacture and sell paper and reconstituted tobacco products to the tobacco industry as well as specialized paper products for use in other applications. Tobacco industry products comprised approximately 93% of our consolidated net sales in each of the years 2009 through 2011. The primary products in the group include cigarette, plug wrap and base tipping papers, or Cigarette Papers, used to wrap various parts of a cigarette and reconstituted tobacco leaf, or RTL, which is used as a blend with virgin tobacco in cigarettes, reconstituted tobacco wrappers and binders for cigars. These products are sold directly to the major tobacco companies or their designated converters in the Americas, Europe, Asia and elsewhere. Non-tobacco products are a diverse mix of products that includes low volume, high-value engineered papers as well as commodity paper grades produced to maximize machine utilization.

We are a manufacturer of lightweight specialty papers, which are used in manufacturing ventilated cigarettes, banded papers for the production of lower ignition propensity, or LIP, cigarettes and the leading independent producer of RTL used in producing blended cigarettes. We conduct business in over 90 countries and currently operate 11 production locations worldwide, with mills in the United States, Canada, France, the Philippines, Indonesia, Brazil and Poland. We also have a 50% equity interest in two joint ventures in China. The first produces cigarette and porous plug wrap papers and the second, which is under construction, will produce reconstituted tobacco leaf.

Our Securities and Exchange Commission, or SEC, filings, which include this Annual Report on Form 10-K, Definitive Proxy Statements on Form DEF-14A, quarterly reports on Form 10-Q, current reports on Form 8-K and all related amendments, are available, free of charge, on the Investor Relations section of our web site at [www.swmintl.com](http://www.swmintl.com). Information from our web site is not incorporated by reference into this Form 10-K. These reports are available soon after they are filed electronically with the SEC. The web site allows access to historical financial information, press releases and quarterly earnings conference calls, our Code of Conduct, corporate governance guidelines, Board of Directors committee charters, as well as disclosure of any amendment to or waivers of our Code of Conduct granted to any of the principal executive officer, principal financial officer or principal accounting officer. The web site provides additional background information about us including information on our history, products and locations. Requests for information or to contact the audit committee chair, lead non-management director or to report concerns about accounting or other issues can be made in writing and sent to the Investor Relations Department at our principal executive office address listed below.

Our quarterly earnings conference calls are typically held the morning after our quarterly earnings releases and are available through our web site via a webcast. The tentative dates for our quarterly earnings conference calls related to 2012 financial results are May 3, 2012, August 2, 2012, November 1, 2012 and February 7, 2013. These dates are subject to change. Instructions on how to listen to the webcasts and updated information on times and actual dates are available through our web site at [www.swmintl.com](http://www.swmintl.com).

Our wholly-owned, majority-owned and controlled subsidiaries are as follows: Schweitzer-Mauduit Canada, Inc., or SM-Canada; Schweitzer-Mauduit Spain, S.L., or SM-Spain, a holding company organized under the Spanish holding company regime and the primary foreign investment holding company for SWM; SWM-Poland, Sp.zo.o., SWM Poland; SWM RTL Philippines Inc.; and Schweitzer-Mauduit International China, Limited, or SM-China, a holding company incorporated in Hong Kong. SM-China owns 50% of the equity interest in China Tobacco Mauduit

(Jiangmen) Paper Industry Company Ltd., (CTM), a Sino-Foreign Equity Joint Venture with China National Tobacco Corporation, or CNTC, to manufacture and sell tobacco-related papers in China and 50% of the equity interest in China Tobacco Schweitzer (Yunnan) Reconstituted Tobacco Co. Ltd., (CTS), a Sino-Foreign Equity Joint Venture to manufacture reconstituted tobacco leaf. Both CTM and CTS are unconsolidated subsidiaries. We indirectly through SM-Spain have subsidiaries in France, the Philippines, Indonesia and Brazil. SM-Spain owns directly 100% of Schweitzer-Mauduit Holding S.A.S., a French holding company, or SMH, and SMH owns 100% of Schweitzer-Mauduit Industries S.A.S., a French corporation, or SMI. Schweitzer-Mauduit International, Inc., SMH and SMI together own 100% of a second holding company Schweitzer-Mauduit France S.A.S., a French corporation, or SMF, which holds our French, Philippine and Indonesian paper operations. SMF directly owns 100% of Schweitzer-Mauduit Developpements S.A.S., a French corporation, or SMD, and SMD owns 100% of LTR Industries S.A.S., a French corporation, or LTRI, our French RTL operation. SMF directly owns 100% of two principal French operating subsidiaries, SWM Services S.A.S. (formerly known as Papeteries de Mauduit S.A.S.), or SWM-S, and Papeteries de Saint-Girons S.A.S., or PdStG, as well as 100% of PDM Philippines Industries, Inc., or PPI, and 95% of P.T. PDM Indonesia, or PT PDM. SMF indirectly owns the third principal French operating subsidiary, PDM Industries S.A.S., or PdM, as well as Papeteries de Malaucène S.A.S., or PdMal, and its subsidiary Malaucène Industries S.A.S., which filed for

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liquidation during December 2011 and are no longer consolidated effective with the date of the filing. SM-Spain also owns directly 99.99% of the issued and outstanding shares of Schweitzer-Mauduit do Brasil S.A., our Brazilian paper operations, or SWM-B. We had no special purpose entities as of December 31, 2011.

Our principal executive office is located at 100 North Point Center East, Suite 600, Alpharetta, Georgia 30022-8246 and our telephone number at that address is 1-800-514-0186. Our stock is traded on the New York Stock Exchange, or NYSE, under the symbol "SWM."

We have provided a Glossary of Terms at the end of this Annual Report on Form 10-K.

## DESCRIPTION OF BUSINESS

**Segment Financial Information.** We operate and manage two reportable segments based on product lines: Paper and Reconstituted Tobacco. The Paper segment primarily produces Cigarette Papers such as cigarette (including LIP), plug wrap and base tipping papers used to wrap various parts of a cigarette for sale to cigarette manufacturers. The Paper segment also includes commercial and industrial products such as lightweight printing and writing papers, battery separator paper, drinking straw wrap, filter paper and other specialized papers. These non-tobacco industry products are generally sold directly to converters and other end-users or brokers. The Reconstituted Tobacco segment produces reconstituted tobacco leaf, or RTL, and wrapper and binder products for sale to cigarette and cigar manufacturers.

Additional information regarding "Segment Performance" is included in Part II, Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operation. In addition, selected financial data for our segments is available in Note 17, Segment Information, of the Notes to Consolidated Financial Statements. Reference is also made to Part I, Item 1A, Risk Factors, Market Risk, for a discussion regarding the risks associated with foreign operations.

Financial information about foreign and domestic operations, contained under the caption "Management's Discussion and Analysis of Financial Condition and Results of Operation" appearing in Part II, Item 7 herein and in Notes 9, 10, 13 and 17 ("Restructuring Activities," "Debt," "Income Taxes" and "Segment Information," respectively) to the Consolidated Financial Statements contained in "Financial Statements and Supplementary Data" appearing in Part II, Item 8 herein, are incorporated in this Item 1 by reference.

## PRODUCTS

We manufacture and sell paper and reconstituted tobacco products to the tobacco industry as well as specialized paper products for use in other applications.

Tobacco industry products include Cigarette Papers and RTL used as a tobacco blend with virgin tobacco in cigarettes and reconstituted tobacco wrappers and binders for cigars. These products are sold directly to tobacco companies or their designated converters in the Americas, Europe, Asia and elsewhere.

Each of the three principal types of Cigarette Papers - cigarette, plug wrap and tipping papers - serves a distinct purpose in the function of a cigarette.

Cigarette paper wraps the column of tobacco in a cigarette. Certain properties of cigarette paper, such as control of ignition propensity, basis weight, porosity, opacity, tensile strength, texture and burn rate must be controlled to tight tolerances. Many of these characteristics are critical to meet the requirements of high-speed production processes utilized by cigarette manufacturers as well as their desired attributes of finished cigarettes such as reduced deliveries of tobacco-related smoke constituents. In addition to the attributes and functional requirements of conventional

cigarette papers, certain of our products facilitate our customers' design of LIP cigarettes to enhance their ability to self-extinguish when they are not actively being smoked, including papers sold under our registered trademark ALGINEX®.

Plug wrap paper forms the outer layer of a cigarette filter and is used to hold the filter materials in a cylindrical form. Conventional plug wrap is manufactured on flat wire paper machines using wood pulp. Porous plug wrap, a highly air-permeable paper, is manufactured on inclined-wire paper machines using a furnish consisting of long-fibers, such as abaca, and wood pulp. Porosity, a measure of air-flow permeability, ranges from a typical level of less than 100 Coresta on conventional plug wrap to 35,000 Coresta on high-porosity papers.



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Base tipping paper, produced in white or tan/cork color, joins the filter element to the tobacco-filled column of the cigarette. The ability to produce tipping paper, which is both printable and glueable at high speeds, is critical to producing a cigarette with a distinctive finished appearance.

Reconstituted tobacco is used by manufacturers of cigarettes and other tobacco products as a means of recycling their tobacco by-products and to achieve product performance attributes. We currently produce reconstituted tobacco in two forms: leaf, or RTL, in France, which is manufactured by LTRI, and wrapper and binder in the United States. RTL is used by cigarette manufacturers primarily to blend with virgin tobacco as a design aid to achieve certain attributes of finished cigarettes, such as taste characteristics and reduced deliveries of tobacco-related smoke constituents, and to cost-effectively utilize tobacco leaf waste by-products. Wrapper and binder are reconstituted tobacco products used by manufacturers of machine-made cigars. Binder is used to hold the tobacco leaves in a cylindrical shape during the production process. Wrapper is used to cover the outside of the cigar, providing a uniform, finished appearance.

Commercial and industrial products include lightweight printing and writing papers, battery separator paper, drinking straw wrap, filter papers and other specialized papers primarily for the western European, North American, Asian and Brazilian markets. Like porous plug wrap, certain of these non-tobacco industry products use a fiber blend consisting of long-fibers. These products are generally sold directly to converters and other end-users in North America and western Europe and through brokers in Brazil. The non-tobacco industry products are a diverse mix that includes low volume, high-value engineered papers as well as commodity paper grades produced to maximize machine utilization.

## MARKETS AND CUSTOMERS

Both segments supply the major, and many of the smaller, cigarette manufacturers including international tobacco companies, regional tobacco manufacturers and government monopolies.

Philip Morris International Inc., or PMI, Philip Morris-USA, a subsidiary of Altria Group Inc., Japan Tobacco Inc., or JTI, and British American Tobacco, or BAT, are our four largest customers and together with their respective affiliates and designated converters, accounted for 54%, 54% and 56% of the Company's 2011, 2010 and 2009 consolidated net sales, respectively. Although the total loss of one or more of these large customers could have a material adverse effect on our results of operations, this is not considered likely given the significant share that our capacity represents of the total worldwide supply available to meet the demand for cigarette-related fine papers. A material variation in demand from one or more of these customers or due to external factors such as government legislation or changes in consumer behavior, however, could result in a significant decline in demand for our products.

## SALES AND DISTRIBUTION

Essentially all tobacco-related products manufactured by both the Paper and Reconstituted Tobacco segments are sold by our marketing, sales and customer service organizations directly to cigarette manufacturers or their designated converters. Most of our Paper Segment's non-tobacco related products, which represent approximately 5% to 8% of its net sales, are sold on a direct basis.

The typical modes of transportation we utilize in the delivery of product to our customers include truck, rail and ocean-going vessels. As is typical in our industry, ownership of the product generally transfers to our customer upon shipment from our mills, except for certain export sales where ownership typically transfers at the foreign port or customer facility.



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COMPETITION

We are the largest producer of Cigarette Papers in the world. LTRI is the leading independent producer of RTL for use in cigarettes. We do not sell our products directly to consumers or advertise our products in consumer media. The specialized nature of these tobacco-related papers requires unique research and development capability and special papermaking equipment and skills to meet exacting customer specifications. These factors have limited the number of competitors in each of the tobacco-related paper categories discussed separately below.

**Cigarette Paper** As the sole domestic producer of Cigarette Papers in North America, we believe that we have the majority supply position. PdM and PdStG, indirect wholly-owned subsidiaries in France, and SWM-Poland sell most of their products in western Europe. We believe SWM-B has the majority of the cigarette paper market in Brazil and in South America. Our principal competitors include European suppliers delfortgroup AG, or Delfort, an Austrian corporation, Miquel y Costas & Miquel S.A., or Miquel y Costas, a Spanish corporation, and Julius Glatz GmbH, an independent German company. The principal competitors of our Indonesian cigarette paper business are PT Surya Zig Zag and PT Bukit Muria Jaya, or PT BMJ, which are owned by Indonesian cigarette production companies. We believe that the bases of cigarette paper competition are price, consistent quality, security of supply, level of technical service and performance requirements of the customer's cigarette-making equipment.

We have developed, individually or in conjunction with customers, technologies to address the market for cigarette paper for LIP cigarettes in the United States, Canada, Australia and the European Union, or EU. We are currently the leading producer of cigarette paper for LIP cigarettes and continue to actively develop the technologies for such products. We have license agreements with third parties which grants them the right to use our LIP intellectual property.

**Plug Wrap Paper** We estimate that our Paper segment holds a majority of market share for plug wrap papers in each of the markets in which we compete. Our competitors are Miquel y Costas and Delfort.

**Base Tipping Paper** Our Paper segment supplies base tipping paper for the North American market, which is subsequently printed by converters. The principal competitors in this market are Delfort and Julius Glatz. We estimate our Brazilian operation holds the majority of the market share for base tipping paper in South America, which is subsequently printed by converters. Our principal competitor in Latin America is Miquel y Costas. We believe that the bases for competition are consistent quality, price and, most importantly, the ability to meet the runability and printability requirements of converting equipment and high-speed cigarette-making machines.

**Reconstituted Tobacco** LTRI is the leading independent producer of RTL in the world. We believe that the basis of competition in this market is primarily quality. However, sales volumes are influenced by worldwide virgin tobacco prices and cigarette producers' various in-house tobacco reconstitution processes, as lower prices of virgin tobacco or other RTL forms may compete against reconstituted tobacco sales volumes.

LTRI's principal competitors are cigarette companies such as Philip Morris-USA, R.J. Reynolds Tobacco Company, Eleks, an affiliate of Japan Tobacco Inc. which operates in Russia, and STMA (China), which produce RTL primarily for internal use. Low prices for tobacco leaf can adversely impact RTL demand.

We estimate that approximately 40% of reconstituted cigar wrapper and binder used in the U.S. market is produced internally by domestic cigar manufacturers. Our Reconstituted Tobacco segment's Ancram mill and Nuway Tobacco, a privately-held cast process manufacturer, produce the balance for the U.S. market which is not produced internally by domestic cigar manufacturers. The Ancram mill and DHT, a subsidiary of NV Deli Maatschappij, are the main suppliers to the European cigar manufacturers.

Other Products We produce papers for lightweight printing and writing, battery separator papers, drinking straw wrap, filter papers and other specialized papers primarily for the western European, North American, Asian and Brazilian markets. We believe that price is the primary basis of competition for drinking straw wrap, printing and writing and filter papers, while consistent quality and customer service are believed to be the primary competitive factors for battery separator paper.

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RAW MATERIALS AND ENERGY

Wood pulp is the primary fiber used in our operations. Our operations consumed 83,000 and 82,000 metric tons of wood pulp in 2011 and 2010, respectively, all of which was purchased. Our operations also use other cellulose fibers, the most significant of which are in the form of flax fiber and tobacco leaf by-products, as the primary raw materials for Cigarette Papers and reconstituted tobacco products, respectively. While tobacco leaf by-products are generally the property of the cigarette manufacturer for whom the reconstitution is contracted, we purchase some tobacco leaf by-products for use in the production of RTL and wrapper and binder products.

Flax straw is purchased and subsequently processed into flax tow at our processing facility in Canada. The flax tow is then converted into flax pulp at pulping facilities in the United States and France or flax pulp may also be purchased on the open market. Certain specialty papers are manufactured by our operations in France, requiring small amounts of other cellulose fibers, all of which are purchased.

In addition to cellulose fibers, our operations use calcium carbonate as another significant raw material in the production of many of our paper products. Calcium carbonate, or chalk, is used in the production of Cigarette Papers, as well as in certain of our other paper products, to provide desired qualities and characteristics, such as opacity, as well as end-product performance attributes. All of our needs for calcium carbonate are purchased. Our Quimperlé mill in France and Pirahy mill in Brazil have on-site, vendor-operated, precipitated calcium carbonate plants which supply significant quantities toward the needs of those mills. For the balance of their needs, our mills also purchase calcium carbonate manufactured elsewhere. Our calcium carbonate purchase commitments are discussed in Note 16, Commitments and Contingencies, of the Notes to Consolidated Financial Statements.

We believe that our purchased raw materials are readily available from several sources and that the loss of a single supplier would not have a material adverse effect on our ability to procure needed raw materials from other suppliers.

The papermaking processes use significant amounts of energy, primarily electricity, natural gas and fuel oil to run the paper machines and other equipment used in the manufacture of pulp and paper. In France, Poland and in the United States, availability of energy is generally not expected to be an issue, although prices can fluctuate significantly. We enter into agreements to procure a portion of our energy requirements for future periods in order to reduce the uncertainty of future energy costs.

In France, we have entered into agreements with an energy cogeneration supplier whereby the supplier constructed and operates cogeneration facilities at our Spay and Quimperlé Mills and supplies steam that is used in the operation of our mills. These cogeneration facilities provide energy cost savings and improved security of supply.

In Brazil, where production of electricity is heavily reliant upon hydroelectric plants, availability of electricity has been affected in the past by rain variations. Our Brazilian business currently has a sufficient supply of energy to continue its current level of operation.

Additional information regarding agreements for the supply of energy is included in Note 16, Commitments and Contingencies, of the Notes to Consolidated Financial Statements.

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### BACKLOG AND SEASONALITY

We have historically experienced a steady flow of orders. Our mills typically receive and ship orders within a 30-day period, except for RTL where orders are generally placed well in advance of delivery. We plan our manufacturing schedules and raw material purchases based on our evaluation of customer forecasts and current market conditions.

Within the Paper segment, the U.S. operations do not calculate or maintain records of order backlogs. Its largest customer Philip Morris-USA provides forecasts of future demand, but actual orders for Cigarette Papers are typically placed two weeks in advance of shipment. In France, Cigarette Papers order backlog was approximately \$30 million and \$28 million on December 31, 2011 and 2010, respectively. This represented approximately 19 and 20 days of sales for the Paper operations in 2011 and 2010, respectively. The Polish and Brazilian operation do not calculate or maintain records of order backlogs. Souza Cruz, Brazil's largest customer, provides forecasts of its future demand, typically eight weeks in advance, in order for the Brazilian operations to manage production and ensure a sufficient supply to meet this customer's anticipated requirements.

The Reconstituted Tobacco segment's RTL business operates predominantly under a number of annual supply agreements. The order backlog for RTL was approximately \$152 million and \$163 million on December 31, 2011 and 2010, respectively.

Sales of our products are subject to significant seasonal fluctuations. In the United States and Europe, customer shutdowns of one to two weeks in duration typically occur in July and December. In Brazil, customer orders are typically lower in December due to a January and February holiday season.

### RESEARCH AND DEVELOPMENT

We employ approximately 60 research and development personnel in research and laboratory facilities in Spay, France, Santanésia, Brazil, San Pedro, Philippines, Strykow, Poland and Alpharetta, Georgia. We are dedicated to developing Cigarette Papers, reconstituted tobacco and non-tobacco paper product innovations and improvements to meet the needs of individual customers. The development of new components for tobacco products and the development of new non-tobacco paper products are the primary focuses of these research and development functions, including several development projects for our major customers. We expensed \$9.3 million in 2011, \$8.5 million in 2010 and \$8.0 million in 2009 on research and development. We believe that our research and product development capabilities have played an important role in establishing our reputation for high quality, superior products.

Our commitment to research and development has enabled us, for example, to (i) produce high-performance papers designed to run on the high-speed manufacturing machines of our customers, (ii) produce papers to exacting specifications with very high uniformity, (iii) produce cigarette paper with extremely low basis weights, (iv) develop cigarette paper for LIP cigarettes, (v) produce highly porous cigarette and plug wrap papers, (vi) produce wrapper and binder tobacco reconstituted products, in a paper process, matching the specifications of machine-made cigars and (vii) produce papers and reconstituted tobacco products with other specifically engineered properties required for end-product performance attributes. We believe that our commitment to research and development, coupled with our investment in new technology and equipment, has positioned us to take advantage of growth opportunities all around the world.

### PATENTS AND TRADEMARKS

As of December 31, 2011, we owned 186 patents and had pending 83 patent applications covering a variety of Cigarette Papers, RTL and cigar wrapper and binder products and processes in the United States, western Europe and several other countries. We believe that such patents, together with our papermaking expertise and technical sales

support, have been instrumental in establishing us as the leading worldwide supplier of Cigarette Papers. We believe that patents have contributed to our position as the world's leading independent producer of papers used for LIP cigarettes.

Management believes that our “ALGINEX®” water-based technology trademark for use in banded papers for the production of LIP cigarettes, and the “SWM” logo and trade names have been important contributors to the marketing of our products.

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### EMPLOYEES

As of December 31, 2011, we had 2,800 regular, full-time, active employees.

North American Operations Hourly employees at the Spotswood, New Jersey, and Ancram, New York mills are represented by locals of the United Steel Workers Union. The collective bargaining agreement at our Spotswood mill is a two-year agreement which is effective through July 28, 2013. The three-year collective bargaining agreement at our Ancram mill is effective through September 30, 2014. We believe employee and union relations continue to be positive at the Spotswood and Ancram mills.

The fiber operations of our Canadian subsidiary and our Newberry, South Carolina facility are non-union. We believe that employee relations are positive.

French Operations Hourly employees at our Quimperlé, Spay, and Saint-Girons, France mills are union represented. Our Quimperlé mill is operating pursuant to an employment agreement that expired effective December 31, 2011. Negotiations are being held at this location regarding compensation issues. The collective bargaining agreements at our Spay and Saint-Girons mills are effective through February 29, 2012 and May 30, 2012, respectively. We believe our employee relations are comparable to similar French manufacturing operations.

Asian Operations Employees of our Philippine operations are non-union. We believe that employee relations in the Philippines are positive.

Our mill in Medan, Indonesia is operating pursuant to a two-year collective bargaining agreement that is effective through June 30, 2012. We believe that employee relations are positive.

Brazilian Operations Hourly employees at the Pirahy mill are represented by a union. The one-year collective bargaining agreement at SWM-B was renewed through May 31, 2012. We believe that employee relations are positive and comparable to similar Brazilian manufacturing operations.

Polish Operations Employees at our Strykow, Poland facility are non-union. We believe that employee relations in Poland are positive.

### ENVIRONMENTAL MATTERS

Capital expenditures for environmental controls to meet legal requirements and otherwise relating to the protection of the environment at our facilities in the United States, France, the Philippines, Indonesia, Brazil and Canada were \$1 million in 2011 and are expected to be \$1 million or less in each of the next two years, of which no material amounts were or are expected to be the result of environmental fines or settlements. These expenditures are not expected to have a material adverse effect on our financial condition, results of operations or competitive position; however, these estimates could be modified as a result of changes in our plans, changes in legal requirements or other factors.

### WORKING CAPITAL

We normally maintain approximately 30 to 60 days of inventories to support our operations. Our sales terms average between 15 and 60 days for payment by our customers, dependent upon the products and markets served. For a portion of our business, particularly our French operation's export sales, extended terms are provided. With respect to our accounts payable, we typically carry approximately a 30 to 60 day level, in accordance with our purchasing terms, which vary by business location. The accounts payable balance varies in relationship to changes in our manufacturing operations, particularly due to changes in prices of wood pulp and purchased energy and the level and timing of



capital expenditures related to projects in progress.

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EXECUTIVE OFFICERS

The names and ages of the Named Executive Officers as of February 24, 2012, together with certain biographical information, are as follows:

Name	Age	Position
Frédéric P. Villoutreix	47	Chairman of the Board and Chief Executive Officer
Otto R. Herbst	52	Chief Operating Officer & Executive Vice President Paper Business
Michel Fievez	54	Executive Vice President, Reconstituted Tobacco Business
Wilfred A. Martinez	58	Vice President, LIP
Jeffrey A. Cook	57	Executive Vice President, Chief Financial Officer and Treasurer
Mark A. Spears	49	Corporate Controller

There are no family relationships between any of the directors, or any of our executive officers. None of our officers were selected pursuant to any arrangement or understanding between the officer and any person other than the Company. Our executive officers serve at the discretion of the Board of Directors and are elected annually by the Board.

Frédéric P. Villoutreix was elected Chairman of the Board and Chief Executive Officer effective January 1, 2009. Mr. Villoutreix joined the Company on December 7, 2005, was elected Chief Operating Officer on February 1, 2006, and served as interim President, French Operations from December 2006 to June 2007. Mr. Villoutreix joined us in December 2005 from Compagnie de Saint-Gobain, a leading French multi-national manufacturer of engineered materials and products, where he worked since 1990. From 2001 to 2005, Mr. Villoutreix held key manufacturing positions in Europe and the United States with Saint-Gobain, including General Manager, World Construction Products and Stone, Luxembourg and Vice President, Abrasives Europe and Coated Abrasives World with 33 operating locations.

Otto R. Herbst has served as Chief Operating Officer since January 2009 and the Executive Vice President Paper Business since March 2010. Previously, Mr. Herbst was President of the Americas beginning in August 2006 with responsibility for the U.S. and Brazilian business units. Mr. Herbst served as our President - Brazilian Operations from April 1999 to July 2006. Prior to April 1999, he served as General Manager for New Business and Services from 1997 through March 1999 for Interprint, a manufacturer of security documents, telephone cards and business forms. From 1990 through 1997, Mr. Herbst served as Director of Agaprint, a manufacturer of packaging materials, business forms, commercial printing papers, personalized documents and envelopes.

Michel Fievez was appointed Executive Vice President Reconstituted Tobacco Business during March 2010. He held the position of President - European Operations from June 2007 to March 2010. From 2003 to May 2007, Mr. Fievez served as General Manager One Side Coated Papers and then Vice President and General Manager Packaging, Metalizing and Office and Graphic with Ahlstrom Corporation. From 1998 to 2003, he held key manufacturing positions, including Managing Director, with Chesapeake Display and Packaging in Europe, and from 1994 to 1998, held the position of Vice President Manufacturing and Technology with Mead Packaging Europe.

Wilfred A. Martinez was appointed Vice President LIP in January 2011. He served as President Americas Paper Business since March 2010. Previously, Mr. Martinez served as President of the Americas from January 1, 2009. Mr. Martinez was Corporate Executive Vice President and Strategy Officer, President, International Division and Senior Vice President, Worldwide Operations from 1996 to 2008 with Laticrete International, Inc., a world leader of tile and stone installation systems. From 1995 to 1996, he was General Manager, Monolithic Refractories, for Harbison-Walker Refractories, Inc., a leading global manufacturer of high temperature refractory products, and from 1979 to 1995 he served as Vice-President, International Operations, Vice-President, Technology and Director, Research and Development for Minteq International, Inc., a technology based multi-national sales and manufacturing

refractory company.

Jeffrey A. Cook was appointed Executive Vice President, Chief Financial Officer and Treasurer in February 2012. Prior to joining SWM, he served as Chief Financial Officer since 2007 of Presstek Inc., a manufacturer and distributor of products for the commercial graphics industry, including printing presses, consumables and service. Mr. Cook began his career with General Electric and served in roles of increasing financial leadership including serving as Chief Financial Officer of GE Government Services Inc. from 1990 to 1993 and Vice President Finance of the Government Services Group of Lockheed Martin Corporation. From 1996 to 1997, he was Vice President and Chief Financial Officer of Bechtel Systems and Infrastructure, a division of Bechtel Group Inc. He was Vice President Finance of Moore North American, a division of Moore Corporation from 1997 to 2000. Mr. Cook served as Senior Vice President Chief Financial Officer and Chief Information Officer of Kodak Polychrome Graphics, a joint venture between Eastman Kodak and Sun Chemical from 2000 to 2005.

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Mark A. Spears has served as our Corporate Controller since March 2008. Mr. Spears served as our interim Chief Financial Officer from November 2011 through February 2012. Mr. Spears joined the Company in 1995 as Corporate Reporting Manager and subsequently served in progressive roles in the Controller department including Director of Corporate Reporting and Assistant Controller. Prior to joining Schweitzer-Mauduit, Mr. Spears was an audit manager with Coopers and Lybrand LLP (now PricewaterhouseCoopers) from 1984 to 1995.

Item 1A. Risk Factors

Factors That May Affect Future Results

Many factors outside our control could impact future financial results. While not an exhaustive list, the following important factors could cause our actual results for 2012 and beyond to differ materially from those expressed in any forward-looking statements we have made.

Our business can be impacted by governmental actions relating to tobacco products.

In 2011, more than 93% of our net sales were from products used by the tobacco industry in making cigarettes or other tobacco products. Governments around the world, particularly in the United States and western Europe, increasingly are regulating the advertising, promotion, sale and use of tobacco products as a result of reports and speculation with respect to the possible harmful physical effects of cigarette smoking, second-hand smoke and use of tobacco products. In addition, tobacco products are heavily taxed in many jurisdictions. Cigarette consumption in the United States and western Europe has declined, in part due to these actions, which, in turn, have decreased demand for our products in these regions. In addition, litigation is pending against the major manufacturers of consumer tobacco products seeking damages for health problems allegedly resulting from the use of tobacco in various forms. It is not possible to predict the outcome of such litigation or what effect adverse developments in pending or future litigation may have on the tobacco industry or its demand for our products, but in the past, increases in taxes and litigation have adversely affected demand. In the U.S., the regulatory jurisdiction of the federal Food and Drug Administration was extended in 2009 to include tobacco products, which are now subject to product component disclosure regulations, new controls on ingredients, and additional restrictions about marketing and labeling. In the European Union, the Tobacco Products Directive regulates the content, effects, marketing and labeling of tobacco products, and the ongoing phase-in of the REACH regulation (Registration, Evaluation, Authorization, and Restriction of Chemical Substances) may further restrict product ingredients. Additionally, the World Health Organization is actively promoting tobacco regulation, and other countries worldwide are in the process of adopting some or all of these restrictions. The impact of these legislative initiatives on the production and sale of our and our customers' products is not presently known.

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Our technological advantages are unlikely to continue indefinitely.

We consider our intellectual property and patents to be a material asset. We have been at the forefront of developing new products and technology within our industry and have patented several of our innovations, particularly with regard to cigarette paper used to produce LIP cigarettes. This has enhanced our ability to sell products and to provide added function and other value to the products we sell allowing them to command higher margins. This advantage has also enabled us to license our patents and know-how and earn royalty income from competitors and customers. Presently, we are seeing evidence of increasing efforts and activity by our competitors to develop and sell competitive products, particularly in the area of papers used for lower ignition propensity applications. Over time, we expect our competitors to develop competitive products that are designed to avoid our patents or to license our innovations. Ultimately, our patents will expire. As we expand our production of LIP papers and RTL to more locations and countries, the risk of the loss of proprietary trade secrets will increase, and any significant loss would result in the loss of the competitive advantages provided by such trade secrets. While we cannot predict the impact or the timing of these trends and eventualities, they likely will reduce our sales and margins from the levels that we otherwise would have achieved.

Effectively policing our domestic and international intellectual property and patent rights is costly and may not be successful.

Our portfolio of granted patents varies by country, which could have an impact on any competitive advantage provided by patents in individual markets. We rely on patent, trademark, and other intellectual property laws of the United States and other countries to protect our intellectual property rights. In order to maintain the benefits of our patents, we may be required to enforce certain of our patents against infringement through judicial or administrative actions. However, we may be unable to prevent third parties from using our intellectual property or infringing on our patents without our authorization, which may reduce any competitive advantage we have developed. If we have to litigate to protect these rights, any proceedings could be costly, time consuming, could divert management resources, and we may not prevail. We cannot guarantee that any United States or foreign patents, issued or pending, will continue to provide us with any competitive advantage or will not be successfully challenged by third parties. We do not believe that any of our products infringe the valid intellectual property rights of third parties. However, we may be unaware of intellectual property rights of others that may cover some of our products or services. In that event, we may be subject to significant claims for damages. Effectively policing our intellectual property and patents is time-consuming and costly, and the steps taken by us may not prevent infringement of our intellectual property, patents or other proprietary rights in our products, technology and trademarks, particularly in foreign countries where in many instances the local laws or legal systems do not offer the same level of protection as in the United States.

In December 2009, Miquel y Costas S.A., delfortgroup AG, and Societe Papeterie Leman SAS filed Notices of Opposition to the European Patent Office's, or EPO, grant of European Patent EP 1482815. The oppositions filed by Societe Papeterie Leman and delfortgroup contend that the claim language regarding the film-forming material to have a certain viscosity was not sufficiently described, that the claims were not patentable due to a prior art reference, a reference that was disclosed by SWM to the examiner and cited by him in granting the patent, and lack of inventive step. Societe Papeterie Leman further alleged that claim 1 is not sufficiently definite and is therefore invalid. Miquel y Costas claims that the patent lacks novelty as to the film-former gum Arabic, that claim 1 of the patent lacks sufficient disclosure and that claim 1 also lacks novelty. The Company will continue to defend the grant of this patent by taking necessary actions including responding to further submissions by the opponents. Once the EPO considers that all positions have been fully briefed, it may hold a hearing to assist it in reaching a final conclusion on the oppositions. There is no mandated timetable by which the EPO must reach a decision. The outcome of this dispute would not prevent the Company from practicing its Alginex® LIP solution. The patent remains in effect and fully enforceable while the opposition proceedings are pending. As a result of a world-wide LIP license agreement reached with SWM in October 2011, delfortgroup withdrew from this proceeding. The action remained open with the other

parties.

On November 12, 2010, the EPO issued a Notice of Decision to Grant SWM European Patent No. 1333729. On December 8, 2010, Julius Glatz GmbH filed a Notice of Opposition to the grant of this patent. In September 2011, Societe Papeterie Leman, Miquel y Costas and delfortgroup each filed opposition papers and Glatz supplemented its previous filing. We expect that the EPO will open an opposition proceeding. The Company believes that the EPO properly granted the patent and it intends to defend the patent should an opposition proceeding be opened. As a result of its world-wide LIP license agreement with SWM, delfortgroup withdrew from this proceeding. The action remained open with the other parties.

The Company filed an infringement action on February 8, 2010 in the United States District Court for South Carolina, Charleston Division, against multiple defendants alleging infringement of the Company's United States Patent Number 6,725,867 and a First Amended Complaint on June 1, 2010 which added claims of alleged infringement under United States Patent Number 5,878,753 and further specifies products we believe violate our patents. Adversarial proceedings present uncertainties and risks, which could include invalidation of the patent in dispute, a change in the scope of the patent claims, or an adverse determination on the question

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of infringement, among others. As was their right under the applicable statute, the defendants requested and the court granted a motion staying this civil action until completion of the International Trade Commission, or ITC, proceedings. The civil action may be restarted once the ITC action is concluded. We believe the outcome of this dispute would not prevent the Company from practicing its Alginex® LIP solution. As a result of the world-wide LIP license agreement, SWM and delfortgroup jointly took action to dismiss delfortgroup from this action. The case is expected to remain open with the other parties, but will remain stayed pending the final determination of the ITC proceeding.

On December 17, 2010, the Company filed a complaint with the ITC against multiple respondents, including Julius Glatz, delfortgroup, Astra Tobacco and LipTEC based on their unlawful importation into the United States, the sale for importation, and the sale within the United States after importation of certain paper wrappers used in manufacture of reduced ignition proclivity cigarettes and products that infringe, are made or produced under, or by means of, a process covered by, one or more of claims 36, 43, and 45 of United States Patent No. 6,725,867 and claims 1-6, 10-18, and 22-25 of United States Patent No. 5,878,753. We amended our complaint to add new respondents including Dosal Tobacco Corp.; Farmer's Tobacco Co.; S M Brands, Inc.; Tantus Tobacco LLC; KenX Worldwide, LLC; Dr. Franz Feurstein GmbH and Paperfabrik Wattens GmbH Co. KG. Our complaint requests the ITC to issue an exclusion order and cease and desist order. The ITC opened an investigation in January 2011, and held hearings October 31, 2011 through November 8, 2011. An initial unfavorable decision was issued by the Administrative Law Judge on February 4, 2012, which we will seek to have reviewed by the full Commission, from which a Target Date for decision is May 29, 2012. During this process, we anticipate that there will be numerous motions, orders and other procedural matters decided that are the normal course of an adversarial process. Absent any of these events having a material impact on the likely outcome of the proceeding, we would not expect to comment on such matters publicly. The outcome of this action will not impact the Company's right to produce and sell its flagship Alginex® papers for LIP cigarettes.

delfortgroup requested re-examinations by the U.S. Patent and Trademark Office, USPTO, of two of our patents: U.S. Patent No. 6,725,867 and U.S. Patent No. 5,878,753. After a number of initial rejections, the USPTO opened an interpartes re-examination of Patent No. 6,725,867 and an ex-parte re-examination of Patent No. 5,878,753. The USPTO issued an initial office action regarding Patent No. 6,725, 867 on March 17, 2011 that confirmed certain claims and that rejected other claims. The timing of the next office action is at the discretion of the USPTO. There can be additional preliminary office actions or a final office action. The patent remains valid and enforceable during the pendency of the re-examination process unless and until a final order of cancellation is issued, which may then be appealed to the Patent Board at the USPTO and thereafter to the U.S. Federal Circuit. The USPTO issued a Notice of Intent to Confirm Patent No. 5,878,753 in September 2011 and on November 1, 2011, the USPTO issued an Ex Parte Reexamination Certificate confirming all claims of Patent No. 5,878,753.

In July 2011, delfortgroup filed an action in the High Court of Justice, Chancery Division, Patents Court in the United Kingdom (UK) seeking a declaration that European Patents (UK) Nos. 0-870-437 and 1-333-729 are each invalid and petitioned for an order that they each be revoked. delfortgroup further petitioned the Court for a declaration under s. 71 Patents Act of 1977 or under the Court's inherent jurisdiction for a declaration that the importation into and sale in the UK of paper wrappers made pursuant to a disclosed process purportedly used by delfortgroup would not constitute an infringement of any of claims 1 to 9 of European Patent (UK) No. 1-333-729. As a result its world-wide LIP license agreement between SWM and the delfortgroup, this proceeding was terminated.

On October 24, 2011, delfortgroup and SWM announced a world-wide non-exclusive patent license agreement that settles their patent disputes over print banded lower ignition propensity papers. Pursuant to this agreement, delfortgroup made a payment to SWM for past sales of LIP print banded product, will pay SWM a minimum annual royalty of \$4 million over the next five years which began with 2011, and a running royalty for the life of the license agreement. This license agreement also settles all of the litigation and administrative proceedings pending between delfortgroup and SWM and, as a result, the proceedings in the U.K. have been terminated. delfortgroup has also

withdrawn from the USPTO re-examination proceedings and European patent opposition proceedings and has been dismissed from the civil infringement action in South Carolina .



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Our financial performance can be significantly impacted by the cost of raw materials and energy.

Raw materials are a significant component of the cost of the paper that we manufacture. The cost of wood pulp, which is the largest component of the raw materials that we use, is highly cyclical and can be more volatile than general consumer or producer inflationary changes in the general economy. For instance, during the period from January 2009 through December 2011, the U.S. list price of northern bleached softwood kraft pulp, or NBSK, a representative pulp grade that we use, ranged from a low of \$635 per metric ton in April 2009 to a high of \$1,010 per metric ton in June 2010. We periodically enter into agreements with customers under which we agree to supply products at fixed prices. As a consequence, unanticipated increases in the costs of raw materials can significantly impact our financial performance. Even where we do not have fixed-price agreements, we generally cannot pass through increases in raw material costs in a timely manner and in many instances are not able to pass through the entire increase to our customers.

Paper manufacturing is energy-intensive. In France, Poland and in the United States, availability of energy generally is reliable, although prices can fluctuate significantly based on variations in overall demand. Western Europe is becoming increasingly dependent on energy supplies from the Commonwealth of Independent States, which in the past has demonstrated a willingness to restrict or cut off supplies of energy to certain customers. The volume of oil or gas flowing through pipeline systems that ultimately connect to western Europe also has been cut off or restricted in the past, and such actions also have the capability of adversely impacting the supply of energy to western Europe. In Brazil, where production of electricity is heavily reliant upon hydroelectric plants, availability of electricity can be, and has in the past been, affected by rain variations. Although our Brazilian business currently has a sufficient supply of energy to continue its current level of operation, there can be no assurance that we will have sufficient supply in the future. Due to the competitive pricing for most of our products, we typically are unable to fully pass through higher energy costs to our customers. Periodically, when we believe it is advantageous to do so, we enter into agreements to procure a portion of our energy for future periods in order to reduce the uncertainty of future energy costs. However, in recent years this has only marginally slowed the increase in energy costs due to the volatile changes in energy prices we have experienced.

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Because of the geographic diversity of our business, we are subject to a range of international risks.

We have manufacturing facilities in seven countries, and sell products in over 90 countries, many of which are emerging and undeveloped markets. Both our manufacturing operations and our sales, depending on their location, are subject to various international business risks, including:

Foreign countries can impose significant tax and other regulatory restrictions on business, including limitations on repatriation of profits and proceeds of liquidated assets. While we evaluate our overall financing plans in the various jurisdictions in which we operate and attempt to manage international movements of cash from and amongst our foreign subsidiaries in a tax-efficient manner, unanticipated international movement of funds due to unexpected changes in our business or in the needs of the business could result in a material adverse impact on our financial condition or results of operations.

We are exposed to changes in foreign currency exchange rates. We utilize a variety of practices to manage this risk, including operating and financing activities and, where considered appropriate, derivative instruments. All derivative instruments we use are either exchange traded or entered into with major financial institutions in order to reduce credit risk and risk of nonperformance by third parties. Counterparty risk cannot be eliminated and there can be no assurance that our efforts will be successful.

Changes in foreign currency exchange rates also impact the amount reported in other income (expense), net. For instance, when a non-local currency receivable or payable is not settled in the period in which it is incurred, we are required to record a gain or loss, as applicable, to reflect the impact of any change in the exchange rate as of the end of the period. We also have to reflect the translation rate impact on the carrying value of our foreign assets and liabilities as of the end of each period, which is recorded as Unrealized Translation Adjustment in Other Comprehensive Income.

We are exposed to global as well as regional macroeconomic and microeconomic factors, which can affect demand and pricing for our products, including: unsettled political and economic conditions; expropriation; import and export tariffs; regulatory controls and restrictions; and inflationary and deflationary economies. Risks inherent in international operations also include risks associated with the U.S. Foreign Corrupt Practices Act and local anti-bribery law compliance.

We participate in two joint ventures in China. One sells our products primarily to Chinese tobacco companies. The second joint venture is building a new reconstituted tobacco mill in China. Operations in China entail a number of risks including international and domestic political risks, the need to obtain operating and other permits from the government and to operate within an evolving legal and economic system.

We are dependent upon the availability of credit, and changes in interest rates can impact our business.

We supplement operating cash flow with bank borrowings under a credit agreement with a syndicate of banks that expires in May 2016. To date, we have been able to access credit when needed and on commercially reasonable terms. However, deterioration of credit markets could have an adverse impact on our ability to negotiate new credit facilities. Constraints on the availability of credit, or the unavailability of credit at reasonable interest rates, would negatively impact our business.

Our credit facility contains financial covenants that we have historically fulfilled, and we do not presently anticipate any events that would impair our ability to meet those covenants in the future. However, in the event of material unforeseen events that impact on our financial performance, particularly during a time when we have material

amounts of debt, a situation could arise where we are unable to fully draw from our existing credit facility notwithstanding that there is otherwise available capacity.

We have a combination of variable and fixed-rate debt consisting of short-term and long-term instruments. We selectively hedge our exposure to interest rate increases on our variable rate long-term debt when we believe that it is practical to do so. We utilize various forms of interest rate hedge agreements, including interest rate swap agreements and forward rate agreements, generally with contractual terms no longer than 24 months. There can be no certainty that our hedging activities will be successful or fully protect us from interest rate exposure.

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Seasonality can impact our business.

Sales of our products in the United States, Europe and Brazil are subject to seasonal fluctuations. In the United States and Europe, customer shutdowns typically occur in July and December and historically have resulted in reduced net sales and operating profit during those two months. Additionally, our mills occasionally shut down equipment to perform additional maintenance during these months, resulting in higher product costs, higher maintenance expenses and reduced operating profit. In Brazil, customer orders are typically lower in December due to a holiday season during much of January and February. As an increasing percentage of our total production capacity and product sales become Asian and southeast Asian based, we will become increasingly subject to seasonal fluctuations that reflect the holiday periods in those regions.

We face competition from several established competitors.

Our three largest competitors are delfortgroup AG, Julius Glatz GmbH and Miquel y Costas. All three primarily operate from modern and cost-effective mills in western Europe and are capable and long-standing suppliers to the tobacco industry. Further, two, Delfort and Glatz, are privately held and the third, Miquel y Costas, is a closely held public company. Thus their financial results and other business developments and strategies are not disclosed to the same extent as ours, which provides them some advantage in dealing with customers. Given our mutual concentration in western Europe, which is a declining market and has labor laws that make reducing capacity expensive and slow, excess capacity exists and therefore price competition is acute. All three have good relationships with the multinational cigarette companies, as does the Company. The multinational cigarette companies have been known to use these close relationships to support development of competitive products and facilities, especially when confronted with high value new technologies such as porous plug wrap in the past and potentially LIP today. As a result of the foregoing, the Company primarily faces selling price, sales volume and new product risks from its existing competitors. Currently, fine papers used to produce cigarettes are not exported from available capacity in China to western multinational cigarette companies due to government taxes which limit price competitiveness. Should conditions change in this regard, capacity that currently is operating in China would present a risk to our competitive position in the developed world. In the RTL market, demand is a function of smoke delivery regulations, the cigarette manufacturer's desire for a uniform and consistent product and the cost of recycling the tobacco by-product scraps relative to the cost of virgin tobacco products. The enhanced capabilities provided by RTL in the area of product design and regulatory compliance are becoming more important to the end-user.

We are dependent upon a small number of customers for a significant portion of our sales. The loss of one or more of these customers could have a materially adverse effect on our business.

Four customers accounted for over 54% of our net sales in 2011. The loss of one or more of these customers, or a significant reduction in their purchases, could have a material adverse effect on our results of operations and financial results. In addition, significant consolidation has occurred among our customers, thereby increasing our dependence upon a fewer number of customers and increasing the negotiating leverage of the customers that survive. Adverse results in the negotiation of any of our significant customer contracts, the terms of which are typically negotiated every one to three years, could significantly impact our financial performance. We are presently the sole supplier of on-line banded cigarette papers for use in LIP cigarettes to Philip Morris-USA for its U.S. requirements under a long-term supply agreement for which Philip Morris-USA is obligated to purchase 100% of its requirements for its proprietary on-line banded cigarette papers for a minimum period of 7 years, and the Company is obligated to supply such product for a minimum of 12 years which began June 1, 2007. This supply agreement is a cost plus arrangement, and Philip Morris-USA began advising us in 2009 that it disagrees with the manner in which we have determined one aspect of the cost of this product as invoiced. Philip Morris-USA has exercised its contract right to have an independent party audit our cost calculation. We have provided Philip Morris-USA with the support for our calculation and confirmed that the calculation was made consistent with methodology applied over the life of the

supply agreement and in accordance with the terms of the supply agreement. This matter could result in litigation between Philip Morris-USA and us. Currently, the amount disputed is approximately \$24.4 million.

Our business is subject to various environmental risks.

Our mills are subject to significant federal, state, local and foreign environmental protection laws with respect to air, water and other emissions as well as the disposal of solid waste. We believe we are operating in substantial compliance with these laws and regularly incur capital and operating expenditures in order to assure future compliance. However, these laws may change in the future, which could require changes in our practices or the incurrence of additional capital expenditures, and we may discover aspects of our business that are not in compliance. Violation of these laws can result in the imposition of significant fines and remediation costs. In France, we presently have sufficient authorized capacity for our emissions of carbon dioxide. However, this authorization must be renewed every five years. We cannot predict that we will have sufficient authorized capacity to conduct our operations in France as presently conducted or to do so without having to make substantial capital expenditures in future years.

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There also is the possibility of regulation of carbon dioxide emissions in the U.S. It is not presently possible to assess what, if any, impact such regulations might have on our domestic U.S. operations.

We are a member of a potentially responsible party group (Global PRP Group) that has entered into a settlement with the State of New Jersey concerning the remediation of a landfill site in Middlesex County, New Jersey. We have established a reserve of less than \$0.1 million that we believe is adequate to cover our liability, but we remain exposed to changes in the State's requirements and in the estimated costs to complete the remediation in accordance with the settlement terms. In 2008, we received an invitation to participate in the remediation of contamination allegedly identified at a mill complex in Elizabeth, New Jersey that was formerly owned and operated by Kimberly-Clark Corporation. Under the terms of our spin-off from Kimberly-Clark in 1995, we are obligated to indemnify Kimberly-Clark Corporation from certain exposures related to the past and future liabilities of the business spun-off, which would include the Elizabeth, New Jersey mill. We declined the invitation to participate in the proposed clean-up of this mill pending the provision of information demonstrating our responsibility to do so, which to date has not been provided.

Although we are not aware of any environmental conditions at any of our facilities that could have a material adverse effect on our financial results, as we sell closed facilities in France and in the U.S. that have been operated over the course of many decades, we may be required to perform additional environmental evaluations that could identify items that might require remediation or other action, the nature, extent and cost of which are not presently known.

We are subject to various legal actions and other claims.

We regularly are involved in legal actions and other claims arising in the ordinary course of business. Although we do not believe that any of the currently pending actions or claims will have a materially adverse impact on our business or financial condition, we cannot provide any assurances in this regard. Information concerning some of the actions that currently are pending is contained in Note 16, Commitments and Contingencies, of the Notes to Consolidated Financial Statements and in Part I, Item 3, "Legal Proceedings".

Our expansion plans entail different and additional risks relative to the rest of our business.

In early 2011, we announced suspension of construction of a wholly-owned reconstituted tobacco mill in the Philippines and plans to construct a new reconstituted tobacco mill in China through a joint venture in which one of our subsidiaries has a 50% ownership interest. Building a new mill is a major construction project and entails a number of risks, ranging from the possibility that the contractors and sub-contractors who are expected to build the facility and supply the necessary equipment do not perform as expected, to the possibility that there will be cost overruns or that design defects or omissions cause the mill to perform at less than projected efficiency or at less than projected capacity. In addition, commencement of production at a new mill is time consuming and requires customer testing and acceptance of the products that are produced. Also, while we anticipate sufficient demand for the mill's output, there can be no assurances that the expected demand will materialize. For more information on our expansion plans, see Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operation.

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Restructuring activities can significantly impact our business.

We began significant restructuring activities in 2006 and 2007 in France and the United States and during 2007 in Brazil that have become part of an overall effort to improve an imbalance between demand for our products and our paper production capacity as well as improve our profitability and the quality of our products. Although now largely completed, restructuring of our existing operations involves issues that are complex, time-consuming and expensive and could significantly disrupt our business. The challenges involved in executing the remaining actions that are part of our restructuring plans include:

- demonstrating to customers that the restructuring activities will not result in adverse changes in service standards or business focus;

- consolidating administrative infrastructure and manufacturing operations while maintaining adequate controls throughout the execution of the restructuring;

- preserving distribution, sales and other important relationships and resolving potential conflicts that may arise;

- minimizing the diversion of management attention from ongoing business activities;

- maintaining employee morale and retaining key employees while implementing restructuring programs that often include reductions in the workforce;

- coordinating and combining operations, which may be subject to additional constraints imposed by collective bargaining agreements and local laws and regulations; and

- achieving the anticipated levels of cost savings and efficiency as a result of the restructuring activities.

In the aggregate including continuing and discontinued operations, we have incurred \$151.5 million in restructuring and related impairment expenses from 2006 through December 31, 2011, including \$91.4 million in cash-related expenses. As a result of actions taken as of December 31, 2011, we expect future payments of approximately \$11 million in cash-related restructuring costs through 2017.

One portion of our business is dependent upon a single mill.

Sales of reconstituted tobacco leaf products represent a substantial portion of our revenues. We presently produce reconstituted tobacco leaf at only one facility located in France. Although reasonable measures have been taken to minimize the risk of a casualty event at this facility, its loss or the interruption of operations for a significant length of time could have a material adverse effect on our business. Our RTL business is also subject to competitive risk from lower cost natural tobacco.

A failure of a key information technology system or process could adversely affect our business.

We rely extensively on information technology systems, some of which are managed by third-party service providers, to analyze, process and manage transactions and data. We also rely heavily on the integrity of this data in managing our business. We or our service providers could experience errors, interruptions, delays or cessations of service in key portions of our information technology infrastructure, which could significantly disrupt our operations and be expensive time-consuming and resource-intensive to remedy.

Item 1B. Unresolved Staff Comments

None.

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Item 2. Properties

As of December 31, 2011, we operated 11 production facilities (which include three fiber pulping operations) on four continents.

We have approximately 133,000 metric tons of annual paper production capacity and approximately 84,000 metric tons of annual reconstituted tobacco products production capacity, dependent upon the production mix. Capacity utilization decreased in 2011 to 90% for paper products and increased to 94% for reconstituted tobacco products compared with 92% and 91%, respectively, in 2010. We also operate flax fiber processing operations in Canada and printing operations in France, Poland and the United States. We own each of these facilities and the associated operating equipment except for a flax tow storage facility in Winkler, Manitoba and the mill building in Strykow, Poland, which are leased.

We maintain administrative and sales offices in Alpharetta, Georgia, in Quimperlé and Spay, France, in Shanghai, China, in Piraí and Rio de Janeiro, Brazil, in San Pedro, Philippines, in Medan, Indonesia, Moscow, Russia and Strykow, Poland. Our world headquarters are also located in Alpharetta. All of these offices are owned except for those located in Alpharetta, Shanghai, Rio de Janeiro, Madrid, Moscow and Strykow.

We consider all of our facilities to be well-maintained, suitable for conducting our operations and business, and adequately insured. The RTL Philippines facility in Sto. Tomas, Philippines is being held in a mothballed state which would require additional construction work before operations commence.

The following are locations of our principal production facilities which are owned, except for the Strykow, Poland facility which is leased, as of December 31, 2011:

Paper Segment	Reconstituted Tobacco Segment
Production Locations	Production Locations
Spotswood Mill	LTR Industries Mill
Spotswood, New Jersey	Spay, France
Papeteries de Saint-Girons Mill	Ancram Mill
Saint-Girons, France	Ancram, New York
Papeteries de Mauduit Mill	RTL Philippines
Quimperlé, France	Sto. Tomas, Philippines
Pirahy Mill	
Piraí, Brazil	
PDM Philippines Industries	
San Pedro, Philippines	
P.T. PDM Indonesia	
Medan, Indonesia	
SWM-Poland	
Strykow, Poland	
Newberry Operation	

Newberry, South Carolina

Fiber Operation  
Manitoba, Canada

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### Item 3. Legal Proceedings

#### General

We are involved in various legal proceedings relating to contracts, commercial disputes, taxes, environmental issues, employment and workers' compensation claims, product liability and other matters. We periodically review the status of these proceedings with both inside and outside counsel. We believe that the ultimate disposition of these matters will not have a material effect on the results of operations in a given quarter or year. Below is a summary of our major outstanding litigation.

#### Litigation

Imposto sobre Circulação de Mercadorias e Serviços, or ICMS, a form of value-added tax in Brazil, was assessed to our Brazilian subsidiary, SWM-B, in December of 2000. SWM-B received two assessments from the tax authorities of the State of Rio de Janeiro for unpaid ICMS taxes from January 1995 through November 2000, collectively the Assessment.

The Assessment concerned the accrual and use by SWM-B of ICMS tax credits generated from the production and sale of certain non-tobacco related grades of paper sold domestically that are immune from the tax to offset ICMS taxes otherwise owed on the sale of products that are not immune. One of the two assessments related in part to tax periods that predated our acquisition of Pirahy and is covered in part by an indemnification from the sellers of Pirahy, or Assessment 1 (case number 2001.001.115144-5). The second assessment pertains exclusively to periods that SWM-B owned the Pirahy mill, or Assessment 2 (case number 2001.001.064544-6). While SWM-B is primarily responsible for the full payment of the Assessment in the event of an ultimate unfavorable outcome, SWM-B is not aware of any difficulties that would be encountered in obtaining reimbursement of that portion of any payment resulting from Assessment 1 from the previous owner under the indemnification.

SWM-B has contested the Assessment based on Article 150, VI of the Brazilian Federal Constitution of 1988, which grants immunity from ICMS taxes to papers used in the production of books, newspapers and periodicals, or immune papers, and the raw material inputs used to produce immune papers.

Both assessments are presently on appeal in separate chambers of the Federal Supreme Court. Assessment 1 is before the court on a procedural question which, if decided favorably, would invalidate Assessment 1. If decided against SWM-B, Assessment 1 would then be sent back to the lower court for a decision on the merits. Assessment 2 is before the Federal Supreme Court on the merits and will be finally decided by the action of the chamber of the court hearing the matter, unless there is a prior decision by a chamber of the Federal Supreme Court on Assessment 2 that is in contradiction, in which case the conflict between the rulings of the different chambers will be decided by the Federal Supreme Court sitting as a whole. No docket entry has been made yet regarding argument on either assessment. SWM-B continues to vigorously contest the Assessment and believes that the Assessment will ultimately be resolved in its favor. Based on the foreign currency exchange rate at December 31, 2011, the Assessment totaled approximately \$44 million, of which approximately \$20 million is covered by the above-discussed indemnification. No liability has been recorded in our consolidated financial statements for the Assessment based on our evaluation of the Assessment under the facts and law as presently understood.

#### Indemnification Matters

In connection with our spin-off from Kimberly-Clark in 1995, we undertook to indemnify and hold Kimberly-Clark harmless from claims and liabilities related to the businesses transferred to us that were not identified as excluded

liabilities in the related agreements. As of December 31, 2011, there are no material claims pending under this indemnification.

Item 4. Mine Safety Disclosures

Not applicable.

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## PART II.

## Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

## Market Information

Since November 30, 1995, our common stock, \$0.10 par value, or Common Stock, has been listed on the New York Stock Exchange, trading under the symbol "SWM." On February 22, 2012, our stock closed at \$69.97 per share.

The table below presents the high and low prices of our Common Stock on the New York Stock Exchange - Composite Transactions reporting system for the periods indicated.

	High	Low
2012		
First Quarter (through February 22, 2012)	\$72.55	\$61.18
2011		
Fourth Quarter	\$74.68	\$53.37
Third Quarter	62.89	50.43
Second Quarter	56.32	47.18
First Quarter	68.38	46.75
2010		
Fourth Quarter	\$69.33	\$53.08
Third Quarter	60.48	42.62
Second Quarter	62.63	47.28
First Quarter	83.63	42.39

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Performance Graph

The following graph compares the total cumulative stockholder return on our Common Stock during the period from December 31, 2006 through December 31, 2011, with the comparable cumulative total returns of the Wilshire 5000 Index and a self-constructed peer group which reflects, but is not exactly comparable to, the Dow Jones Paper Products Index. We have selected the following companies as our peer group: Neenah Paper Inc., P.H. Glatfelter Co., Wausau Paper Corp., and Buckeye Technologies Inc.

The graph assumes that the value of the investments in the Common Stock and each index were \$100 on December 31, 2006 and that all dividends were reinvested. The stock price performance shown on the graph below is not necessarily indicative of future price performance.

Comparison of Cumulative Five Year Total Return  
Holders

As of February 22, 2012, there were 2,593 stockholders of record.

Dividends

We have declared and paid cash dividends of \$0.15 per share of our Common Stock every fiscal quarter since the second quarter of 1996. We currently expect to continue this level of quarterly dividend. Our Credit Agreement covenants require that we maintain certain financial ratios, as disclosed in Note 10, Debt, of the Notes to Consolidated Financial Statements, none of which under normal business conditions materially limit our ability to pay such dividends. We will continue to assess our dividend policy in light of our cash generation, debt levels and ongoing requirements for cash to fund operations and to pursue possible strategic opportunities.

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## Securities Authorized for Issuance under Equity Compensation Plans

The following table provides information, as of December 31, 2011, with respect to the shares of our Common Stock that may be issued under our existing equity compensation plans:

Plan Category	Number of Securities To be Issued Upon Exercise of Outstanding Options	Weighted-Average Price of Outstanding Options	Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans (Excluding securities reflected in the first column)
Equity Compensation Plans approved by stockholders:			
Equity Participation Plan <sup>(1)</sup>	104,950	\$ 32.02	—
Outside Directors Stock Plan <sup>(2)</sup>	N/A	N/A	65,923
Restricted Stock Plan <sup>(3)</sup>	N/A	N/A	673,440
Total approved by stockholders	N/A	N/A	739,363
Equity Compensation Plans not approved by stockholders:			
Grand Total	—	—	—
	N/A	N/A	739,363

N/A - Not applicable.

(1) The Equity Participation Plan is described in Note 15, Stockholders' Equity, of the Notes to Consolidated Financial Statements appearing in Part II, Item 8 herein.

(2) The Outside Directors Stock Plan consists of shares registered for the purpose of issuance to our outside Directors for payment of their retainer fees quarterly in advance. Director's retainer fees in 2011 were \$15,000 quarterly which are payable in our Common Stock. The number of shares issued each quarter is determined based on the then fair market value of the shares, which is determined in accordance with the plan as closing price on the date one day prior to the date of distribution. Certain Directors have elected to defer receipt of quarterly retainer fees under the terms of our Deferred Compensation Plan for Non-Employee Directors, resulting in an accumulation of stock unit credits. The Director has the option, upon retirement or earlier termination from the Board of Directors, to have these stock unit credits distributed in the form of our Common Stock or cash. While held in the deferred compensation plan account, these stock unit credits carry no voting rights and cannot be traded as Common Stock, although declared dividends create additional stock unit credits. As of December 31, 2011, deferred retainer fees have resulted in 38,760 accumulated stock unit credits, excluding credited dividends (43,562 accumulated stock unit credits including credited dividends).

(3) The Restricted Stock Plan is described in Note 15, Stockholders' Equity, of the Notes to Consolidated Financial Statements appearing in Part II, Item 8 herein. Shares awarded under the terms of this plan are both subject to forfeiture and cannot be sold or otherwise transferred until fully vested or such restrictions are otherwise lifted. Such shares are deemed by us to be issued and outstanding and are subject to all other financial interests, including our declared dividends. As of December 31, 2011, 179,653 shares issued under this plan remained restricted.

## Recent Sales of Unregistered Securities

We had no unregistered sales of equity securities during the fiscal year ended December 31, 2011.





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## Repurchases of Equity Securities

The following table indicates the number of shares and amount of our Common Stock repurchased during 2011 and the remaining number of shares and amount of share repurchases currently authorized by our Board of Directors as of December 31, 2011:

	Total Number Of Shares Repurchased	Average Price Paid Per Share	Total Number of Shares Repurchased As Part of Publicly Announced Programs  (# shares)	(\$ in millions)	Maximum Amount Of Shares that May Yet be Repurchased Under the Program  (\$ in millions)
First Quarter	803,337	\$ 57.09	525,000	\$ 30.0	
Second Quarter	1,143,469	51.29	1,143,469	58.7	
Third Quarter	293,390	56.22	291,741	16.3	
October	—	—	—	—	
November	—	—	—	—	
December	—	—	—	—	
Fourth Quarter	—	—	—	—	
Full Year 2011	2,240,196	\$ 53.59	1,960,210	\$ 105.0	\$ 50.0

In December 2011, the Board of Directors authorized the repurchase of shares of SWM Common Stock during the period December 2, 2011 to December 31, 2012 in an amount not to exceed \$50.0 million. Under the current \$50 million authorization for 2012 share repurchases, the Company purchased 235,105 shares for \$16.1 million as of February 22, 2012.

The Company sometimes uses corporate 10b5-1 plans so that share repurchases can be made at predetermined stock price levels, without restricting such repurchases to specific windows of time. Future Common Stock repurchases will be dependent upon various factors, including the stock price, strategic opportunities and cash availability.

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## ITEM 6. Selected Financial Data

The following selected financial data should be read in conjunction with Item 7, “ Management's Discussion and Analysis of Financial Condition and Results of Operation,” and the consolidated financial statements and related notes within this Annual Report on Form 10-K. The results of our closed Malaucène, France mill have been retrospectively presented as discontinued operations for all periods and have been deconsolidated effective with a liquidation filing in December 2011 due to a loss of control. All dollar amounts are in millions except per share amounts, statistical data and ratios.

	For the Years Ended December 31,					
	2011	2010	2009	2008	2007	
<b>Results of Operations</b>						
Net Sales	\$816.2	\$740.2	\$719.6	\$724.5	\$676.4	
Cost of products sold	575.7	543.6	531.8	617.9	565.3	
Gross Profit	240.5	196.6	187.8	106.6	111.1	
Nonmanufacturing expenses	91.4	73.6	74.7	60.2	62.2	
Valuation allowance on business tax credits	15.9	—	—	—	—	
Restructuring & impairment expense	14.0	13.4	23.9	6.5	18.7	
Operating Profit	119.2	109.6	89.2	39.9	30.2	
Income from Continuing Operations	87.6	71.4	59.6	16.7	20.0	
Income (Loss) from Discontinued Operations	5.0	(6.1 )	(24.0 )	(15.8 )	(8.6 )	
Net Income	92.6	65.3	35.6	0.9	11.4	
Net Income Attributable to Noncontrolling Interest	—	—	—	0.2	8.0	
Net Income (Loss) Attributable to SWM	\$92.6	\$65.3	\$35.6	\$0.7	\$3.4	
<b>Net Income (Loss) Per Share- Basic:</b>						
Income from continuing operations	\$5.20	\$3.94	\$3.80	\$1.06	\$0.77	
Income (loss) from discontinued operations	0.30	(0.34 )	(1.53 )	(1.02 )	(0.55 )	
Net income (loss) per share - Basic	\$5.50	\$3.60	\$2.27	\$0.04	\$0.22	
<b>Net Income (Loss) Per Share - Diluted:</b>						
Income from continuing operations	\$5.16	\$3.86	\$3.69	\$1.05	\$0.77	
Income (loss) from discontinued operations	0.30	(0.33 )	(1.49 )	(1.01 )	(0.55 )	
Net income (loss) per share - Diluted	\$5.46	\$3.53	\$2.20	\$0.04	\$0.22	
Cash Dividends Declared and Paid Per Share	\$0.60	\$0.60	\$0.60	\$0.60	\$0.60	
EBITDA from Continuing Operations (Earnings before interest, taxes, depreciation and amortization) (1)	\$145.8	\$145.8	\$128.0	\$74.4	\$71.5	
Adjusted EBITDA from Continuing Operations (1)	\$159.2	\$159.2	\$151.9	\$80.9	\$90.2	
<b>Percent of Net Sales</b>						
Gross Profit	29.5	% 26.6	% 26.1	% 14.7	% 16.4	%
Nonmanufacturing expenses	11.2	% 9.9	% 10.4	% 8.3	% 9.2	%
<b>Financial Position</b>						
Capital spending	\$60.9	\$73.7	\$15.3	\$35.3	\$47.7	
Depreciation	36.9	33.0	37.1	41.0	39.9	
Total Assets	841.9	850.4	791.9	728.7	775.0	
Total Debt	146.0	51.8	60.1	179.8	100.9	
Total debt to capital ratio (1)	23.5	% 9.0	% 11.1	% 39.3	% 21.5	%

Earnings before interest, taxes, depreciation and amortization (EBITDA) from Continuing Operations is a non-GAAP financial measure that is calculated by adding interest expense, income tax provision, net income attributable to controlling interest, depreciation and amortization expense to income (loss) from continuing operations. Adjusted

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EBITDA from continuing operations is a non-GAAP financial measure that is calculated by adding restructuring and impairment expense to EBITDA from continuing operations. The Company believes investors' understanding of the Company's performance is enhanced by disclosing these non-GAAP financial measures as a reasonable basis for comparison of the Company's ongoing results of operations. Reconciliations to income from continuing operations are as follows (\$ in millions):

	For the Years Ended December 31,				
	2011	2010	2009	2008	2007
Income from Continuing Operations	\$87.6	\$71.4	\$59.6	\$16.7	\$20.0
Plus: Interest expense	2.6	1.8	4.3	9.5	5.3
Plus: Tax provision (benefit)	31.1	39.8	25.3	6.4	5.0
Plus: Depreciation and amortization	43.6	40.0	43.9	47.4	39.2
Less: Amortization of deferred revenue	(6.0 )	(7.2 )	(5.1 )	(5.8 )	(6.0 )
Plus: Net income attributable to noncontrolling interest	—	—	—	0.2	8.0
EBITDA from Continuing Operations	158.9	145.8	128.0	74.4	71.5
Plus: Valuation allowance on business tax credits	15.9	—	—	—	—
Plus: Restructuring and impairment expense	14.0	13.4	23.9	6.5	18.7
Adjusted EBITDA from Continuing Operations	\$188.8	\$159.2	\$151.9	\$80.9	\$90.2

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Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following is a discussion of our results of operations and financial condition. This discussion should be read in conjunction with our consolidated financial statements and related notes included elsewhere in this report and the selected financial data included in Item 6. The discussion of our results of operations and financial condition includes various forward-looking statements about our markets, the demand for our products and our future prospects. These statements are based on certain assumptions that we consider reasonable. For information about risks and exposures relating to us and our business, you should read the section entitled "Factors That May Affect Future Results," in Part I, Item 1A of this Form 10-K.

The Management's Discussion and Analysis of Financial Condition and Results of Operation is designed to provide a reader of our financial statements with an understanding of our recent performance, our financial condition and our prospects. The following will be discussed and analyzed:

Summary

Recent Developments

Critical Accounting Policies and Estimates

Recent Accounting Pronouncements

Administrative and Court Proceedings Relating to Papers for Lower Ignition Propensity Cigarettes

Results of Operations

Liquidity and Capital Resources

Other Factors Affecting Liquidity and Capital Resources

Outlook

Forward-Looking Statements

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### Summary

In 2011, SWM reported net income of \$92.6 million on total net sales of \$816.2 million.

Benefiting from the advent of the LIP compliance in the EU during the fourth quarter, sales in 2011 increased 7 percent at constant currency, confirming the positive trend reported in the prior year.

Diluted earnings per share in 2011 increased 63 percent to \$5.46, compared to \$3.53 in 2010, despite unfavorable impacts from higher pulp prices and currency exchange rates.

Cash provided by operations was \$81.5 million in 2011, compared to \$141.1 million in the prior year. The lower cash generation during 2011 was largely due to a planned increase in working capital, which used \$24.0 million of cash in 2011, primarily reflecting new working capital needs to support operations in Poland, compared to a net working capital reduction in 2010 which generated \$28.3 million of cash. This \$52.3 million swing accounted for most of the reduction in cash provided by operations. Our 2011 strategic investments in higher-value products included \$11 million to complete construction of the LIP facility in Poland and \$31 million constructing an RTL facility in the Philippines to a mothball state until we decide to re-initiate its operations. Other 2011 cash uses were an additional equity contribution of \$6.2 million to our Chinese Paper joint venture, CTM, and the first \$6.0 million of an expected total of approximately \$30 million to our Chinese RTL joint venture, CTS. We expect to make the remaining contributions to CTS as it begins construction of its RTL facility. We also returned \$105 million to investors through open market stock repurchases during 2011.

Return on invested capital (ROIC) increased to 20 percent in 2011, compared to 17 percent in 2010. This measure, at the core of our executive compensation plans, reflects our determination to invest in products, projects and businesses that consistently yield returns in excess of our underlying cost of capital.

### Recent Developments

During 2011, the Company executed a joint venture contract with affiliates of China National Tobacco Corporation to form a joint venture to manufacture RTL in Yuxi, Yunnan Province in China named China Tobacco Schweitzer (Yunnan) Reconstituted Tobacco Co. Ltd., or CTS. SWM will own 50% of the venture. SWM's 50% equity contribution is expected to total approximately \$30 million and will be financed using its current credit facilities and cash generated from operations. The Company began contributing to the venture in the fourth quarter of 2011. After a two-year construction period, SWM expects the joint venture will begin production in 2014.

Cigarette manufacturers completed actions to meet the LIP requirements in the European Union in 2011 and we continue to strengthen our market position in this premium application and to realize improvement in the margin profile of our Paper segment. During 2011, we expanded sales of LIP papers from our new LIP facilities in Europe and achieved profitable operations at our new Poland facility despite incurring \$6.5 million in start-up costs.

In October 2011, SWM and delfortgroup jointly announced entry into a world-wide, non-exclusive patent license agreement regarding the production and sale of print banded LIP cigarette paper and settlement of all litigation and administrative proceedings pending between us and delfort. The agreement, which was effective immediately, will continue concurrent with the enforceable life of SWM's licensed patents, which expire in the normal course between 2014 and 2023. The license agreement provides for a guaranteed annual minimum royalty of \$4 million for each of the first five calendar years commencing in 2011 and running royalties as well as an amount to settle any claims related to past sales. During 2011, the Company recognized \$17.0 million in royalty income from this and other patent

royalty agreements.

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### Critical Accounting Policies and Estimates

Our consolidated financial statements are prepared in conformity with accounting principles generally accepted in the United States, which require management to make estimates that affect the amounts of revenues, expenses, assets and liabilities reported and disclosure of contingencies. Changes in these estimates could have a significant impact on our results of operations, financial position, or cash flows. We discussed with the Audit Committee of the Board of Directors the estimates and judgments made for each of the following items and our accounting for and presentation of these items in the accompanying financial statements:

#### Accounting for Income Taxes

We must make assumptions, judgments and estimates to determine our current provision for income taxes and also our deferred income tax assets and liabilities and any valuation allowance to be recorded against a deferred income tax asset. Our judgments, assumptions and estimates take into account our interpretation of current tax laws. Changes in tax law or our interpretation of tax laws could significantly impact the amounts provided for income taxes in our consolidated financial statements. Our assumptions, judgments and estimates relative to the value of a deferred tax asset take into account projections of the amount and category of future taxable income. Actual operating results and the underlying amount and category of income in future years could render our current assumptions, judgments and estimates of recoverable net deferred taxes inaccurate. Any of the assumptions, judgments and estimates mentioned above could cause our actual income tax obligations to differ from our estimates, thus materially impacting our financial position and results of operations.

We have available net operating loss carryforwards, or NOLs, and other various tax credits in the jurisdictions in which we operate, for which we have recorded deferred tax assets totaling \$49.3 million and \$12.7 million, respectively, as of December 31, 2011. We record and maintain income tax valuation allowances to reduce deferred tax assets to an amount we estimate will be realizable more likely than not. Our deferred tax asset valuation allowances are primarily the result of uncertainties regarding the future realization of recorded tax benefits on tax loss carryforwards for certain entities. As a result, at December 31, 2011, we have \$12.7 million of valuation allowances against certain of the deferred tax assets.

Expiration periods vary for our NOLs depending on the tax laws governing the jurisdiction where the NOL was generated. Under current tax laws, remaining NOLs in France and Brazil carry forward indefinitely, and NOLs in Spain expire in 15 years subsequent to the year generated. We have recorded a valuation allowance to fully reserve certain deferred tax assets in Brazil, since we believe that we will not generate sufficient taxable income in Brazil within an acceptable period of time given the annual utilization limitation of 30% of taxable income.

We expect sufficient future taxable income in France and the Philippines to fully utilize the respective French and Philippine NOL carryforward deferred tax assets, net of valuation allowances, and plan to utilize available tax planning strategies in France. The Company's assumptions, judgments and estimates relative to the valuation of these net deferred tax assets take into account available positive and negative evidence of realizability, including recent financial performance, the ability to realize benefits of restructuring and other recent actions, projections of the amount and category of future taxable income and tax planning strategies. Actual future operating results and the underlying amount and category of income in future periods could differ from the Company's current assumptions, judgments and estimates. Although realization is not assured, the Company believes it is more likely than not that these net deferred tax assets at December 31, 2011, will be realized. Future operating losses in Brazil, the Philippines and the Company's paper operations in France could result in recording additional valuation allowance in a future period which could be material to our results of operations in the period that such valuation allowance was recorded. If at a future date the Company determines that the weight of the positive evidence is not sufficient to overcome the negative evidence, additional valuation allowances against these deferred tax assets to reduce the net deferred tax asset



to an amount we believe will more likely than not be realizable would be recorded in the period such determination is made.

The Company was granted certain tax incentives in Poland for investment in a special economic zone. These incentives are in the form of credits granted in 2011 that will offset qualified taxable income through 2020. Based on granted incentives, commitments achieved, including maintaining certain employment levels, and qualified investment through December 31, 2011, the Company has a \$11.7 million deferred tax asset at December 31, 2011. We expect to be able to fully utilize these credits by 2013.

At December 31, 2011 and 2010, we had no significant unrecognized tax benefits related to income taxes. Changes in tax laws or interpretations of tax laws, as well as outcomes of current and future audits conducted by foreign and domestic tax authorities, could materially impact the amounts provided for income taxes in our consolidated financial statements.

For additional information regarding income taxes and valuation allowances, see Note 13, Income Taxes, of the Notes to Consolidated Financial Statements.

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### Accounting for Contingencies

We accrue an estimated loss by taking a charge to income when the likelihood that a future event, such as a legal proceeding, will result in a loss or the incurrence of a liability is probable and the amount of loss can be reasonably estimated. We disclose material contingencies if there is at least a reasonable possibility that a loss has been incurred. In determining whether a loss should be accrued, we evaluate, among other factors, the degree of probability of an unfavorable outcome and the ability to make a reasonable estimate of the amount of loss. Changes in these factors could materially impact our results of operations, financial position, or our cash flows.

For further information, please see “Litigation” in Part I, Item 3, “Legal Proceedings” and Note 16, Commitments and Contingencies, of the Notes to Consolidated Financial Statements.

### Property, Plant and Equipment Valuation

Paper manufacturing, which is our primary manufacturing process, is a capital intensive process. As a result, we make substantial investments in property, plant and equipment which are recorded at cost. Net property, plant and equipment comprised 51% of our total assets as of December 31, 2011. Property, plant and equipment is depreciated on the straight-line method over the estimated useful lives of the assets. Paper machines and related equipment are not subject to substantial technological changes rendering them obsolete and are generally depreciated over estimated useful lives of 20 years. In the United States, banded cigarette paper production assets at the Spotswood Mill are generally depreciated over estimated useful lives of 10 years. When indications of impairment exist, we assess the likelihood of recovering the cost of long-lived assets based on our expectation of future profitability and undiscounted cash flow of the related operations. These factors, along with management's plans with respect to the operations, are considered in assessing the recoverability of property, plant and equipment. Changes in management's estimates and plans could significantly impact our results of operations, financial position or cash flows.

As a result of excess capacity in the tobacco-related papers industry and increased purchased material and operating costs experienced in the last several years, competitive selling prices for certain of our products are not sufficient to cover our costs with a reasonable margin. Such competitive pressures have resulted in downtime of certain paper machines and, in some cases, accelerated depreciation or impairment of certain equipment. Over the past four years, we have restructured our operations to improve our competitiveness and profitability. As a result, we incurred significant charges related to asset impairments, accelerated depreciation and employee severances. Due to the closure of our mill in Malaucène, France, the activities of Malaucène have been retrospectively presented as a discontinued operation and as a result of filing for liquidation in December 2011, the financial position of Malaucène has been deconsolidated.

Certain of our Spotswood Mill's banded cigarette paper production assets remain underutilized and likely would otherwise be shut down except that we have a contractual commitment to stand ready to produce commercial quantities of banded cigarette paper for a customer. Certain of the infrastructure improvements and other assets installed to be able to produce commercial quantities of banded cigarette paper would still be used by a scaled down operation even if we stopped manufacture of that product. As of December 31, 2011, the net book value of Spotswood Mill property, plant and equipment was \$35.6 million of which \$5.4 million related to three paper machines capable of producing banded cigarette paper but not currently in operation.

In 2011, the Company revised its Asian RTL expansion plans and suspended the construction of the Philippine greenfield site. Due to this change, the carrying value of partially constructed assets is evaluated for impairment at each reporting period by assessing the recoverability of the costs based on the undiscounted cash flows of the operation, likelihood of its reactivation and alternative uses for the equipment. The net book value of the RTL Philippines property, plant and equipment was \$71.9 million as of December 31, 2011. An impairment loss, measured

by comparing the projected carrying value of the completed assets to their fair value as determined by discounted cash flows, potential alternative uses and appraised market prices, of \$3.3 million was recorded during 2011 for certain equipment requiring rework.

Management continues to evaluate how to operate our production facilities more effectively with reduced tobacco-related papers volumes. Further restructuring actions are possible that might require additional write-offs or accelerated depreciation of some equipment.

#### Recent Accounting Pronouncements

For a discussion regarding recent accounting pronouncements, see “Recent Accounting Pronouncements” included in Note 2, Summary of Significant Accounting Policies, of the Notes to Consolidated Financial Statements.

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Administrative and Court Proceedings Relating to Papers for Lower Ignition Propensity Cigarettes

In December 2009, Miquel y Costas S.A., delfortgroup AG, and Societe Papeterie Lemman SAS filed Notices of Opposition to the European Patent Office's, or EPO, grant of European Patent EP 1482815. The oppositions filed by Societe Papeterie Lemman and delfortgroup contend that the claim language regarding the film-forming material to have a certain viscosity was not sufficiently described, that the claims were not patentable due to a prior art reference, a reference that was disclosed by SWM to the examiner and cited by him in granting the patent, and lack of inventive step. Societe Papeterie Lemman further alleged that claim 1 is not sufficiently definite and is therefore invalid. Miquel y Costas claims that the patent lacks novelty as to the film-former gum Arabic, that claim 1 of the patent lacks sufficient disclosure and that claim 1 also lacks novelty. The Company will continue to defend the grant of this patent by taking necessary actions including responding to further submissions by the opponents. Once the EPO considers that all positions have been fully briefed, it may hold a hearing to assist it in reaching a final conclusion on the oppositions. There is no mandated timetable by which the EPO must reach a decision. The outcome of this dispute would not prevent the Company from practicing its Alginex® LIP solution. The patent remains in effect and fully enforceable while the opposition proceedings are pending. As a result of the recently announced world-wide LIP license agreement with SWM, delfortgroup has withdrawn from this proceeding. The action will remain open with the other parties.

On November 12, 2010, the EPO issued a Notice of Decision to Grant SWM European Patent No. 1333729. On December 8, 2010, Julius Glatz GmbH filed a Notice of Opposition to the grant of this patent. In September 2011, Societe Papeterie Lemman, Miquel y Costas and delfortgroup each filed opposition papers and Glatz supplemented its previous filing. We expect that the EPO will open an opposition proceeding shortly. The Company believes that the EPO properly granted the patent and it intends to defend the patent should an opposition proceeding be opened. As a result of the recently announced world-wide LIP license agreement with SWM, delfortgroup has withdrawn from this proceeding. The action will remain open with the other parties.

The Company filed an infringement action on February 8, 2010 in the United States District Court for South Carolina, Charleston Division, against multiple defendants alleging infringement of the Company's United States Patent Number 6,725,867 and a First Amended Complaint on June 1, 2010 which added claims of alleged infringement under United States Patent Number 5,878,753 and further specifies products we believe violate our patents. Adversarial proceedings present uncertainties and risks, which could include invalidation of the patent in dispute, a change in the scope of the patent claims, or an adverse determination on the question of infringement, among others. As was their right under the applicable statute, the defendants requested and the court granted a motion staying this civil action until completion of the International Trade Commission, or ITC, proceedings. The civil action may be restarted once the ITC action is concluded. We believe the outcome of this dispute would not prevent the Company from practicing its Alginex® LIP solution. As a result of the recently announced world-wide LIP license agreement, delfortgroup has been dismissed from this action. The case is expected to remain open with the other parties, but will remain stayed pending the final determination of the ITC proceeding.

On December 17, 2010, the Company filed a complaint with the ITC against multiple respondents, including Julius Glatz, delfortgroup, Astra Tobacco and LipTEC based on their unlawful importation into the United States, the sale for importation, and the sale within the United States after importation of certain paper wrappers used in manufacture of reduced ignition propensity cigarettes and products that infringe, are made or produced under, or by means of, a process covered by, one or more of claims 36, 43, and 45 of United States Patent No. 6,725,867 and claims 1-6, 10-18, and 22-25 of United States Patent No. 5,878,753. The ITC opened an investigation in January 2011, and a hearing before the Administrative Law Judge resulted in an initial decision published on February 1, 2012, that held that the '753 patent was valid but the asserted claims were not infringed by the respondents and the respondents infringed the asserted claims of the '867 but those claims were invalid. The Company will petition the ITC for a review of the initial decision and has a right to appeal a final ITC decision to the Circuit Court of Appeal for the Federal Circuit. During

the remainder of the ITC process, we anticipate that there will be numerous motions, orders and other matters decided that are the normal course of an adversarial process. Absent any of these events having a material impact on the likely outcome of the proceeding, we would not expect to comment on such matters publicly. The outcome of this action will not impact the Company's right to produce and sell its flagship Alginex® papers for LIP cigarettes.

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delfortgroup requested re-examinations by the U.S. Patent and Trademark Office, USPTO, of two our patents: U.S. Patent No. 6,725,867 and U.S. Patent No. 5,878,753. After a number of initial rejections, the USPTO opened an interpartes re-examination of Patent No. 6,725,867 and an ex-parte re-examination of Patent No. 5,878,753. The USPTO issued an initial office action regarding Patent No. 6,725, 867 on March 17, 2011 that confirmed certain claims and that rejected other claims. The timing of the next office action is at the discretion of the USPTO. There can be additional preliminary office actions or a final office action. The patent remains valid and enforceable during the pendency of the re-examination process unless and until a final order of cancellation is issued, which may then be appealed to the Patent Board at the USPTO and thereafter to the Circuit Court of Appeal for the Federal Circuit. The USPTO issued a Notice of Intent to Confirm Patent No. 5,878,753 in September 2011 and on November 1, 2011, the USPTO issued an Ex Parte Reexamination Certificate confirming all claims of Patent No. 5,878,753.

In July 2011, delfortgroup filed an action in the High Court of Justice, Chancery Division, Patents Court in the United Kingdom (UK) seeking a declaration that European Patents (UK) Nos. 0-870-437 and 1-333-729 are each invalid and petitioned for an order that they each be revoked. delfortgroup further petitioned the Court for a declaration under s. 71 Patents Act of 1977 or under the Court's inherent jurisdiction for a declaration that the importation into and sale in the UK of paper wrappers made pursuant to a disclosed process purportedly used by delfortgroup would not constitute an infringement of any of claims 1 to 9 of European Patent (UK) No. 1-333-729. As a result of the world-wide license agreement with the delfortgroup, this action has been terminated.

On October 24, 2011, delfortgroup and SWM announced a world-wide non-exclusive patent license that settles their patent disputes over print banded lower ignition propensity papers. Pursuant to this agreement, delfortgroup will pay SWM a minimum annual royalty of \$4 million over the next five years, a payment for past sales of LIP print banded product and a running royalty for the life of the license agreement. This license agreement also settles all of the litigation and administrative proceedings pending between delfortgroup and SWM as a result of which delfortgroup has withdrawn or been dismissed from all such proceeding and, where delfortgroup was the only party, such proceedings have been terminated.

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## Results of Operations

	For the Years Ended December 31,			
	2011	2010	2009	
	(\$ in millions, except per share amounts)			
Net Sales	\$816.2	\$740.2	\$719.6	
Cost of products sold	575.7	543.6	531.8	
Gross Profit	240.5	196.6	187.8	
Selling expense	22.0	19.0	19.4	
Research expense	9.3	8.5	8.0	
General expense	60.1	46.1	47.3	
Total nonmanufacturing expenses	91.4	73.6	74.7	
Valuation allowance on ICMS business tax credits	15.9	—	—	
Restructuring and impairment expense	14.0	13.4	23.9	
Operating Profit	119.2	109.6	89.2	
Interest expense	2.6	1.8	4.3	
Other income (expense), net	(2.6	) 0.2	(1.1	)
Income from Continuing Operations Before Income Taxes and Loss from Equity Affiliates	114.0	108.0	83.8	
Provision for income taxes	31.1	39.8	25.3	
Income from equity affiliates	4.7	3.2	1.1	
Income from Continuing Operations	87.6	71.4	59.6	
Income (loss) from Discontinued Operations	5.0	(6.1	) (24.0	)
Net Income	\$92.6	\$65.3	\$35.6	
Net Income Per Share - Basic:				
Income per share from continuing operations	\$5.20	\$3.94	\$3.80	
Income (loss) per share from discontinued operations	0.30	(0.34	) (1.53	)
Net income per share - basic	\$5.50	\$3.60	\$2.27	
Net Income Per Share - Diluted:				
Income per share from continuing operations	\$5.16	\$3.86	\$3.69	
Income (loss) per share from discontinued operations	0.30	(0.33	) (1.49	)
Net Income per share - diluted	\$5.46	\$3.53	\$2.20	

## Discontinued Operations

The results of the closed tipping mill in Malaucène, France have been classified as a discontinued operation. As a result, all periods presented have been retrospectively recast to exclude the discontinued operations. During the fourth quarter of 2011, the Malaucène mill entered liquidation resulting in a loss of control for accounting consolidation purposes. The net deficit of Malaucène has been removed from the consolidated accounts resulting in recognition of a \$6.4 million net gain, approximately \$0.38 per diluted share. Malaucène's results of operations were included in the Company's discontinued operations through the date of the liquidation filing. The \$6.1 million loss in 2010 from discontinued operations was the result of severance being accrued over the remaining service period of the affected employees, impairment losses on certain assets and inventory and accruals for certain site clean-up costs. In 2009, the \$24.0 million loss from discontinued operations was the result of severance accruals, asset impairments and accelerated depreciation as a result of the decision to close the mill.





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Year Ended December 31, 2011 Compared with the Year Ended December 31, 2010

## Net Sales

(dollars in millions)

	2011	2010	Change	Percent Change	Consolidated Sales Volume Change
Paper	\$579.3	\$516.6	\$62.7	12.1	% (6 )%
Reconstituted Tobacco	236.9	223.6	13.3	5.9	(1 )
Total	\$816.2	\$740.2	\$76.0	10.3	% (4 )%

Net sales were \$816.2 million in 2011 compared with \$740.2 million in 2010. The increase in net sales consisted of the following (dollars in millions):

	Amount	Percent	
Changes due to sales volume	\$48.1	6.5	%
Changes in currency exchange rates	21.9	3.0	
Changes due to royalty income	17.0	2.3	
Changes in product mix and selling prices	(11.0)	(1.5)	)
Total	\$76.0	10.3	%

Unit sales volumes decreased by 4% in 2011 versus the prior year. Despite lower overall volumes, the \$48.1 million impact of sales volume changes was favorable since the dollar impact of higher-value products offset the dollar impact of traditional products.

Sales volumes for the Paper segment decreased by 6%. Sales volume for traditional tobacco-related paper products declined in certain markets partially offset by a 40% increase in LIP paper sales volume and increased sales of mostly low-margin, non-tobacco paper products to utilize available paper machine time. The dollar impact of increased LIP volumes more than offset the dollar impact of the decline in traditional paper volume.

Sales volumes in the Reconstituted Tobacco segment decreased by 1% primarily due to reduced orders from certain major customers. Sales volumes during 2011 declined and were in line with previously announced demand decreases from two of our largest customers.

Changes in currency exchange rates increased net sales by \$21.9 million, or 3%, in 2011 and primarily reflected the impact of changes in the value of the euro compared with the U.S. dollar in 2011 versus the prior year.

During 2011, the Company began receiving royalties on certain of its LIP patents. The \$17.0 million of 2011 royalty income included a \$4 million annual minimum payment, a settlement of past sales and 2011 running royalties from our agreements.

Unfavorable changes in selling prices and sales mix negatively impacted sales by \$11.0 million.

Paper segment 2011 net sales of \$579.3 million increased by \$62.7 million, or 12.1%, versus \$516.6 million in 2010. The increase in net sales was primarily the result of \$46.1 million impact of increased volumes of high-value products, \$17.0 million of royalty income and \$12.0 million in favorable foreign exchange impacts mostly due to changes in the value of the euro compared to the U.S. dollar partially offset by \$12.4 million in unfavorable sales mix.

Reconstituted Tobacco segment 2011 net sales of \$236.9 million increased by \$13.3 million, or 5.9%, compared with \$223.6 million in 2010. The increase in net sales of the Reconstituted Tobacco segment resulted from \$9.9 million favorable foreign currency impact of changes in the value of the euro versus the U.S. dollar, \$2.0 million of favorable impact of sales volumes, mostly for our wrapper and binder products, and \$1.4 million favorable product mix and higher selling prices.



Table of ContentsOperating Expenses  
(dollars in millions)

	2011	2010	Change	Percent Change	Percent of Net Sales		
					2011	2010	
Net Sales	\$816.2	\$740.2	\$76.0	10.3	% 100.0	% 100.0	%
Cost of products sold	575.7	543.6	32.1	5.9	70.5	73.4	
Gross Profit	\$240.5	\$196.6	\$43.9	22.3	% 29.5	% 26.6	%

Higher 2011 gross profit versus 2010 was due to \$34.8 million higher sales volume impacts, primarily due to the effectiveness of EU LIP legislation in the fourth quarter, \$15.4 million lower manufacturing costs primarily due to benefits from our operating excellence and lean manufacturing initiatives and \$17.0 million of royalty income from third-party license agreements. These positives were partially offset by a \$16.8 million increase in inflationary costs, primarily related to energy, and \$6.5 million of start-up expenses related to European LIP. Pulp prices moderated over the course of 2011 but on average remained higher than in 2010. The average per ton list price of northern bleached softwood kraft pulp in the United States was \$980 per metric ton during 2011 compared with \$960 per metric ton during 2010.

Nonmanufacturing Expenses  
(dollars in millions)

	2011	2010	Change	Percent Change	Percent of Net Sales		
					2011	2010	
Selling expense	\$22.0	\$19.0	\$3.0	15.8	% 2.7	% 2.5	%
Research expense	9.3	8.5	0.8	9.4	1.1	1.1	
General expense	60.1	46.1	14.0	30.4	7.4	6.3	
Nonmanufacturing expenses	\$91.4	\$73.6	\$17.8	24.2	% 11.2	% 9.9	%

Nonmanufacturing expenses in 2011 increased by \$17.8 million to \$91.4 million from \$73.6 million in 2010, including higher legal expenses to defend SWM LIP patents of approximately \$10 million and higher expenses to support expansion of LIP in the EU.

## Valuation Allowance on ICMS Business Tax Credits

In 2011, the Company recorded a \$15.9 million valuation allowance against the entire carrying value of its Imposto sobre Circulação de Mercadorias e Serviços, or ICMS, business tax credits in Brazil. The Company had been seeking a special government action to obtain tax exempt status for the paper industry to enable more rapid utilization of these credits. During the third quarter of 2011, the government of Rio de Janeiro state signed into law an action; however, the action included certain limitations on the use of these credits for the paper industry and has a finite life of 48 months. As a result, utilization of the Company's credits may be delayed barring other changes outside of the Company's control. The credits do not expire. The Company is still pursuing other actions to utilize its credits.

## Restructuring and Impairment Expense

The Company incurred total restructuring and impairment expense of \$14.0 million in 2011 which included in the Paper segment \$7.1 million for employee severance and other cash costs and \$6.9 million impairment charges on fixed assets. In the Reconstituted Tobacco segment, the Company incurred \$4.6 million impairment and other costs to suspend construction of the RTL facility in the Philippines. In 2010, the Company's restructuring and impairment expense was \$13.4 million, including \$9.1 million for employee severance and other cash costs and \$4.3 million for asset and goodwill impairment charges, accelerated depreciation and other non-cash charges.



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## Operating Profit

(dollars in millions)

	2011	2010	Change	Percent Change	Return on Net Sales		
					2011	2010	
Paper	\$49.0	\$37.6	\$11.4	30.3	% 8.5	% 7.3	%
Reconstituted Tobacco	90.3	89.2	1.1	1.2	38.1	39.9	
Unallocated expenses	(20.1	) (17.2	) (2.9	)			
Total	\$119.2	\$109.6	\$9.6	8.8	% 14.6	% 14.8	%

Operating profit was \$119.2 million in 2011 compared with \$109.6 million during the prior year.

The Paper segment's 2011 operating profit was \$49.0 million, an increase of \$11.4 million from 2010. The increase was primarily due to the following factors:

\$34.6 million in favorable sales volumes

\$17.0 million in royalty income

\$9.1 million in benefits from operational excellence, lean manufacturing initiatives and lower manufacturing costs

These positive factors were partially offset by a \$15.9 million valuation allowance to fully reserve the Company's ICMS business tax credits, \$12.2 million in higher inflationary costs such as energy, labor and materials prices, \$10 million in higher litigation expenses, \$6.5 million in European LIP start-up expenses and \$6.4 million in unfavorable foreign exchange impacts primarily related to the Brazilian real and U.S. dollar exchange rates.

The Reconstituted Tobacco segment's 2011 operating profit was \$90.3 million, a \$1.1 million increase from \$89.2 million in 2010. The increase was primarily due to:

\$5.7 million in decreased manufacturing costs as a result of our operational excellence and lean manufacturing initiatives

\$3.8 million from foreign currency exchange impacts primarily due to a weaker U.S. dollar relative to the euro

- These positive factors were partially offset by \$4.6 million in increased inflationary costs and \$4.4 million in higher restructuring costs for the suspended RTL Philippines facility

## Non-Operating Expenses

Interest expense was \$2.6 million in 2011, an increase from \$1.8 million in 2010. The increase in interest expense is due to higher average outstanding debt balances and higher interest rates. During 2011 the Company entered into a new, larger debt facility. The Company capitalized \$1.5 million and \$0.7 million of interest expense in 2011 and 2010, respectively, related to the construction of the RTL facility in the Philippines and the EU LIP facility in Poland. The weighted average effective interest rates on our debt facilities were approximately 2.0% and 1.7% for 2011 and 2010, respectively.

Other expense, net in 2011 was \$2.6 million and other income, net was \$0.2 million in 2010, primarily due to foreign currency transaction impacts and interest income.



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### Income Taxes

A \$31.1 million provision for income taxes in 2011 reflected an effective tax rate of 27.3% compared with 36.9% in 2010. The 2011 effective tax rate was lower than the statutory rate primarily due to the Company's Polish operations which were granted certain tax incentives for investment in a special economic zone. These incentives were in the form of credits that will offset qualified taxable income for a limited period of time. Based on granted incentives, commitments achieved, including maintaining certain employment levels and qualified investment through December 31, 2011, the Company has available credits for which we recorded deferred income tax benefits of \$11.7 million. These credits are currently expected to be fully utilized by 2013, after which we expect to pay income taxes at approximately the 19% Polish statutory income tax rate. In 2011, the Company recorded a \$5.9 million valuation allowance to fully reserve its net deferred tax assets in Brazil. In 2010, the provision for income taxes included a \$1.9 million valuation allowance that reduced the deferred tax asset for net operating loss carryforwards in Brazil.

### Income from Equity Affiliates

Income from equity affiliates was \$4.7 million in 2011 compared with \$3.2 million during 2010. These results reflected the operations of our joint venture in China to produce cigarette papers. The improved results reflect the joint venture's increased sales volume and favorable sales mix, including new products.

### Discontinued Operations

Operations at our Malaucène mill are reported as discontinued operations for all periods presented. Consequently, results of the Malaucène mill have been removed from each line of the statements of income and the operating activities section of the statements of cash flow. In each case, a separate line has been added for the net results of the discontinued operation, including previously reported restructuring and impairment amounts. During the fourth quarter of 2011, a Malaucène liquidation petition resulted in a loss of control for accounting consolidation purposes. The net deficit of Malaucène has been removed from the consolidated accounts of the Company as of the date of liquidation resulting in recognition of a gain of approximately \$6.4 million, or \$0.38 per diluted share.

### Net Income and Income per Share

Net income in 2011 was \$92.6 million, or \$5.46 per diluted share, compared with \$65.3 million, or \$3.53 per diluted share, during 2010. The increase in net income in 2011 was primarily due to royalty income, increased sales in Europe upon the effectiveness of LIP regulations, recording deferred tax benefits for Poland's tax incentives, and a net gain on the deconsolidation of Malaucène. These positives were partially offset by higher inflationary costs, valuation allowance on ICMS business taxes, higher legal expenses, start-up expenses for European LIP manufacturing and unfavorable currency exchange impacts.

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Year Ended December 31, 2010 Compared with the Year Ended December 31, 2009

## Net Sales

(dollars in millions)

	2010	2009	Change	Percent Change	Consolidated Sales Volume Change	
Paper	\$516.6	\$496.3	\$20.3	4.1	% 1.1	%
Reconstituted Tobacco	223.6	223.3	0.3	0.1	(0.6	)
Total	\$740.2	\$719.6	\$20.6	2.9	% 0.4	%

Net sales in 2010 were \$740.2 million compared with \$719.6 million in 2009. The increase in net sales consisted of the following (dollars in millions):

	Amount	Percent	
Changes in product mix and selling prices	\$23.5	3.3	%
Changes due to volume	6.3	0.9	
Changes in currency exchange rates	(9.2	) (1.3	)
Total	\$20.6	2.9	%

Changes in product sales mix consisting of more high-value products such as LIP papers in the Paper segment and RTL products in the Reconstituted Tobacco segment had a favorable \$23.5 million, or 3.3% , impact on the net sales comparison.

Increase in unit sales volumes in 2010 versus 2009 resulted in a favorable effect on net sales of \$6.3 million, or 0.9%. Unit sales volumes increased by 0.4% in 2010 versus 2009.

Sales volumes for the Paper segment increased by 1.1%. Sales volumes of traditional tobacco-related papers continued to decline in certain markets but were more than offset by increased sales of banded cigarette papers and non-tobacco papers primarily produced to fill available machine time.

Sales volumes in the Reconstituted Tobacco segment decreased by 0.6% primarily due to decreased demand from certain of SWM's major customers.

Changes in currency exchange rates decreased net sales by \$9.2 million, or 1.3%, in 2010 compared to 2009 and primarily reflected the impacts of changes in the value of the euro and Brazilian real compared with the U.S. dollar during 2010 versus the prior year.

Paper segment 2010 net sales of \$516.6 million increased by \$20.3 million, or 4.1%, versus \$496.3 million in 2009. The increase in net sales was primarily the result of \$14.0 million favorable impact of product mix and \$6.0 million favorable impact of higher sales volumes.

Reconstituted Tobacco segment 2010 net sales of \$223.6 million increased by \$0.3 million, or 0.1%, compared with \$223.3 million in 2009. The increase in net sales of the Reconstituted Tobacco segment resulted from the \$9.5 million favorable impact of product mix and higher selling prices mostly offset by an unfavorable \$9.4 million effect of foreign currency changes in the value of the euro versus the U.S. dollar.





Table of ContentsOperating Expenses  
(dollars in millions)

	2010	2009	Change	Percent Change	Percent of Net Sales 2010	Percent of Net Sales 2009	
Net Sales	\$740.2	\$719.6	\$20.6	2.9	% 100.0	% 100.0	%
Cost of products sold	543.6	531.8	11.8	2.2	73.4	73.9	
Gross Profit	\$196.6	\$187.8	\$8.8	4.7	% 26.6	% 26.1	%

Gross profit in 2010 was \$196.6 million, an increase of \$8.8 million, or 4.7%, from \$187.8 million for 2009. The gross profit margin in 2010 was 26.6% of net sales, increasing from 26.1% in 2009. Gross profit was favorably impacted by \$21.6 million from cost saving programs and \$7.1 million from higher average selling prices due to an improved mix of products sold. These favorable impacts were partially offset by \$16.1 million in inflationary increases, primarily wood pulp. The average per ton list price of northern bleached softwood kraft pulp in the United States was \$960 in 2010 compared with \$720 per metric ton in 2009.

Nonmanufacturing Expenses  
(dollars in millions)

	2010	2009	Change	Percent Change	Percent of Net Sales 2010	Percent of Net Sales 2009	
Selling expense	\$19.0	\$19.4	\$(0.4)	(2.1)%	2.7	2.6	%
Research expense	8.5	8.0	0.5	6.3	1.1	1.1	
General expense	46.1	47.3	(1.2)	(2.5)%	7.1	6.1	
Nonmanufacturing expenses	\$73.6	\$74.7	\$(1.1)	(1.5)%	10.9	9.8	%

Nonmanufacturing expenses in 2010 decreased by \$1.1 million, or 1.5%, to \$73.6 million from \$74.7 million in 2009, primarily due to lower accruals for incentive expenses. Nonmanufacturing expenses were 9.9% and 10.4% of net sales in 2010 and 2009, respectively.

## Restructuring and Impairment Expense

The Company incurred total restructuring and impairment expense of \$13.4 million in 2010, including \$9.1 million for employee severance and other cash costs and \$4.3 million for asset and goodwill impairment charges, accelerated depreciation and other non-cash charges. Total restructuring expense of \$23.9 million was recognized in 2009, including \$12.2 million for employee severance and other cash costs and \$11.7 million for asset impairment charges, accelerated depreciation and other non-cash charges.

Operating Profit  
(dollars in millions)

	2010	2009	Change	Percent Change	Return on Net Sales 2010	Return on Net Sales 2009	
Paper	\$37.6	\$31.1	\$6.5	20.9	% 7.3	% 6.3	%
Reconstituted Tobacco	89.2	79.8	9.4	11.8	39.9	35.7	
Unallocated expenses	(17.2)	(21.7)	4.5				
Total	\$109.6	\$89.2	\$20.4	22.9	% 14.8	% 12.4	%

Operating profit in 2010 was \$109.6 million compared with \$89.2 million in 2009.

The Paper segment's 2010 operating profit was \$37.6 million, an increase of \$6.5 million from 2009. The increase was primarily due to \$11.3 million in improved manufacturing expenses and the benefits of cost savings programs and \$9.6 million in lower restructuring and impairment costs. These positive factors were partially offset by \$15.8 million in higher inflationary cost increases mostly as a result of higher wood pulp costs.

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The Reconstituted Tobacco segment's 2010 operating profit was \$89.2 million, a \$9.4 million increase from \$79.8 million in 2009. The increase was primarily due to a \$9.5 million impact from a favorable mix of products sold and higher selling prices, \$3.1 million in improved manufacturing expenses and the benefits of cost savings programs. These were partially offset by \$3.6 million in unfavorable foreign currency impacts primarily from the euro versus the U.S. dollar.

### Non-Operating Expenses

Interest expense of \$1.8 million in 2010 decreased from \$4.3 million in 2009. Average debt levels decreased significantly during 2010 versus 2009, mainly due to higher operating cash flow and a portion of the November 2009 equity offering proceeds which were used to pay down debt. The weighted average effective interest rates on our debt facilities were approximately 1.7% and 1.9% for 2010 and 2009, respectively.

Other expense, net was income of \$0.2 million in 2010 compared to expense of \$1.1 million in 2009. The favorable change is primarily due to \$1.0 million of lower net foreign currency transaction losses in 2010 compared to 2009 and interest income.

A \$39.8 million income tax provision was recognized for 2010 compared to \$25.3 million income tax provision recognized in 2009. The effective tax rate was 36.9% and 30.2% in 2010 and 2009, respectively. Both periods were impacted by tax benefits from substantial restructuring and impairment expenses and our foreign holding company structure which reduced the effective tax rate from statutory rates. In 2010, higher pre-tax income is the primary cause of the higher expense. In 2010, the provision includes a \$1.9 million valuation allowance against certain net operating loss carryforwards. In 2009, we incurred \$1.0 million in deferred tax expense as a result of a legal reorganization during 2008 and a decision by management to consider the undistributed earnings of LTRI to be permanently reinvested.

### Income from Equity Affiliates

The income from equity affiliates in 2010 was \$3.2 million compared with \$1.1 million in 2009 and represents our 50% share of the net income associated with our joint venture paper mill in China.

### Net Income and Net Income per Share

Net income in 2010 was \$65.3 million, or \$3.60 and \$3.53 per basic and diluted share, respectively, compared with \$35.6 million of net income, or \$2.27 and \$2.20 per basic and diluted share in 2009, respectively. The increase in net income in 2010 was primarily due to a higher proportion of RTL and LIP products in the sales mix, higher average selling prices and benefits of strategic actions taken in prior years to reduce manufacturing costs.

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## Liquidity and Capital Resources

A major factor in our liquidity and capital resource planning is our generation of cash flow from operations, which is sensitive to changes in the sales mix, volume and pricing of our products, as well as changes in our production volumes, costs and working capital. Our liquidity is supplemented by funds available under our revolving credit facility with a syndicate of banks that is used as either operating conditions or strategic opportunities warrant. As of December 31, 2011, \$69.8 million of the Company's \$76.5 million of cash and cash equivalents was held by foreign subsidiaries. Movement of cash balances may have significant tax consequences. The Company considers the undistributed earnings of its foreign subsidiaries to be indefinitely reinvested and currently plans to repatriate such earnings only when tax effective to do so. We believe that we are able to maintain a sufficient level of liquidity for our domestic operations and commitments without repatriation of the cash held by these foreign subsidiaries.

Capital spending for 2012 is currently projected to be approximately \$35 million. Other cash needs, including approximately \$30 million funding of the RTL joint venture in China and \$10 million for shareholder dividends, are projected to range between \$40 and \$50 million. We plan to fund our capital projects using cash on-hand, cash generated from operations and our existing credit facilities. Under the current \$50 million authorization for 2012 share repurchases, the Company purchased 235,105 shares for \$16.1 million as of February 22, 2012.

## Cash Requirements

As of December 31, 2011, we had net operating working capital of \$98.8 million and cash and cash equivalents of \$76.5 million, compared with net operating working capital of \$47.4 million and cash and cash equivalents of \$87.3 million as of December 31, 2010. Changes in these amounts include the impacts of changes in currency exchange rates and excess tax benefits of stock-based awards which are not included in the changes in operating working capital presented on the consolidated statements of cash flow.

Cash Flows from Operating Activities (\$ in millions)	For the Years Ended December 31,		
	2011	2010	2009
Net Income	\$92.6	\$65.3	\$35.6
Less: Loss from discontinued operations	5.0	(6.1)	(24.0)
Income from continuing operations	87.6	71.4	59.6
Non-cash items included in net income:			
Depreciation and amortization	43.6	40.0	43.9
Restructuring-related impairment	6.8	4.5	12.1
Valuation allowance on ICMS business tax credits	15.9	—	—
Amortization of deferred revenue	(6.0)	(7.2)	(5.1)
Deferred income tax provision	(15.9)	25.4	22.0
Pension and other postretirement benefits	(6.5)	2.1	(20.6)
Stock-based compensation	3.8	7.7	8.2
Income from equity affiliates	(4.7)	(3.2)	(1.1)
Excess tax benefits of stock-based awards	(10.0)	(1.6)	(3.3)
Other items	(2.9)	(3.4)	1.2
Net changes in operating working capital	(24.0)	28.3	(39.4)
Net cash provided by operating activities of:			
Continuing operations	87.7	164.0	77.5
Discontinued operations	(6.2)	(22.9)	(14.1)
Cash Provided by Operations	\$81.5	\$141.1	\$63.4

Net cash provided by operations was \$81.5 million in 2011 compared with \$141.1 million in 2010. Our net cash provided by operations changed unfavorably by \$59.6 million in 2011 compared to the prior year primarily due to \$24.0 million unfavorable changes in operating working capital in 2011 versus favorable changes in operating working capital in 2010 of \$28.3 million, a change of \$52.3 million.

Net cash provided by operations was \$141.1 million in 2010 compared with \$63.4 million in 2009. The \$77.7 million increase in 2010 was due to increased net income, improved working capital and lack of contributions to our U.S. pension and other postretirement plans compared to \$27.3 million in contributions in 2009.

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Prior to 2002, our cash provided by operations included advance payments from customers for future product purchases. We recorded these advance payments as deferred revenue, which was amortized into net sales as earned and credited to customers based upon a mutually agreed-upon amount per unit of product sales. The remaining \$6.0 million of deferred revenue on our December 31, 2010 consolidated balance sheet was fully amortized in 2011.

Operating Working Capital (\$ in millions)	For the Years Ended December 31,		
	2011	2010	2009
Changes in operating working capital			
Accounts receivable	\$(25.8 )	\$(15.8 )	\$1.8 )
Inventories	(4.5 )	9.9	(10.2 )
Prepaid expenses	0.5	(0.1 )	1.2 )
Accounts payable	(4.5 )	17.4	(17.9 )
Accrued expenses	2.1	(5.5 )	10.6 )
Accrued income taxes	8.2	22.4	(24.9 )
Net changes in operating working capital	\$(24.0 )	\$28.3	\$(39.4 )

In 2011, net changes in operating working capital contributed unfavorably to cash flow by \$24.0 million. The change in working capital was primarily driven by initiation of operations in Poland to support European LIP sales.

In 2010, net changes in operating working capital were favorable to cash flow by \$28.3 million, primarily due to receipt of a \$20 million tax refund in France and higher accounts payable. These increases were partially offset by increases in accounts receivable.

In 2009, net changes in operating working capital was unfavorable to cash flow by \$39.4 million, primarily due to lower accrued income taxes as a result of estimated income tax payments in France which were refunded in 2010 and lower accounts payable in part as a result of a 2009 French law limiting vendor payment terms to 60 days. Partially offsetting these increases in working capital, accrued expense increased primarily from restructuring-related severance accruals.

Cash Flows from Investing Activities (\$ in millions)	For the Years Ended December 31,		
	2011	2010	2009
Capital spending	\$(60.9 )	\$(73.7 )	\$(15.3 )
Capitalized software costs	(1.3 )	(9.3 )	(5.5 )
Investment in equity affiliates	(12.2 )	—	—
Other	2.3	1.8	0.6
Cash Used for Investing	\$(72.1 )	\$(81.2 )	\$(20.2 )

Cash used for investing activities in 2011 was \$72.1 million and was primarily capital spending to bring the RTL-Philippines site to its mothball state. The Company made equity contributions of \$12.2 million to its joint ventures in China including \$6.2 million to its existing paper joint venture CTM and an initial contribution of \$6.0 million to its RTL joint venture.

During 2011, the Company entered into an agreement with the affiliates of China National Tobacco Corporation to form a joint venture to manufacture RTL in Yuxi, Yunnan Province in China named China Tobacco Schweitzer (Yunnan) Reconstituted Tobacco Co. Ltd., or CTS. SWM owns 50% of the venture. SWM's 50% equity contribution is expected to total approximately \$30 million and will be financed using its current credit facilities and cash

generated from operations. After a two-year construction period, SWM expects the joint venture will begin production in 2014.

During 2010, cash used for investing activities was due to capital spending of \$73.7 million related to constructing an RTL facility in the Philippines and an LIP facility in Poland. The Company also spent \$9.3 million for capitalized software costs substantially all of which was to implement new enterprise-wide information software in the U.S., Brazil and Poland.



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## Capital Spending and Capitalized Software Costs

Capital spending was \$60.9 million, \$73.7 million and \$15.3 million in 2011, 2010 and 2009, respectively. The capital spending incurred during 2011 and 2010 was primarily due to \$30.8 million and \$35.9 million, respectively, for construction of a reconstituted tobacco facility in the Philippines and \$9.2 million and \$15.8 million in 2011 and 2010, respectively, to establish an LIP production facility for the EU in Poland.

Capitalized software costs were \$1.3 million, \$9.3 million and \$5.5 million for 2011, 2010 and 2009, respectively, substantially all of which was to implement an enterprise-wide information system in the U.S., Brazil and Poland. Capitalized software costs in 2009 also included \$3.2 million for completion of implementation of an enterprise-wide information system.

We incur spending necessary to meet legal requirements and otherwise relating to the protection of the environment at our facilities in the United States, France, the Philippines, Indonesia, Brazil, Canada and Poland. For these purposes, we expect to incur capital expenditures of approximately \$1 million in 2012 and less than \$1 million in 2013, of which no material amount is the result of environmental fines or settlements. The foregoing capital expenditures are not expected to reduce our ability to invest in other appropriate and necessary capital projects and are not expected to have a material adverse effect on our financial condition or results of operations.

Cash Flows from Financing Activities (\$ in millions)	For the Years Ended December 31,		
	2011	2010	2009
Cash dividends paid to SWM stockholders	\$(10.1 )	\$(10.8 )	\$(9.6 )
Net proceeds from (payments on) borrowings	100.5	(4.8 )	(122.5 )
Issuances of common stock	—	—	117.4
Purchases of treasury stock	(120.9 )	(19.0 )	(0.8 )
Proceeds from exercises of stock options	2.2	2.2	13.3
Excess tax benefits of stock-based awards	10.0	1.6	3.3
Cash Used in Financing	\$(18.3 )	\$(30.8 )	\$1.1

During 2011, financing activities included \$120.9 million of repurchases, including open market purchases and surrendering of vested restricted stock by employees to satisfy tax withholding, net borrowings of \$100.5 million and excess tax benefits of the vesting of stock-based awards of \$10.0 million. Cash dividends paid to SWM stockholders were \$10.1 million.

During 2010, financing activities included \$19.0 million of share repurchases, \$10.8 million in cash dividends paid to SWM stockholders, repayments of debt of \$56.3 million and net borrowings of \$51.5 million.

Financing activities during 2009 included net borrowings of \$33.5 million and repayments of \$156.0 million. In November 2009, the Company completed a secondary stock offering and received net proceeds of \$117.4 million. Other 2009 financing activities included proceeds from stock option exercises of \$13.3 million for which we received \$3.3 million of tax benefits, cash dividends of \$9.6 million paid to SWM stockholders as well as \$0.8 million of share repurchases.

## Dividend Payments

We have declared and paid cash dividends of \$0.15 per share of our Common Stock every fiscal quarter since the second quarter of 1996. We currently expect to continue this level of quarterly dividend. Our Credit Agreement covenants require us to maintain certain financial ratios, as disclosed in Note 10, Debt, of the Notes to Consolidated Financial Statements, none of which under normal business conditions materially limit our ability to pay such

dividends.

On February 1, 2012, we announced that the Board of Directors had declared a quarterly cash dividend of \$0.15 per share of Common Stock. The dividend will be payable on March 22, 2012 to stockholders of record on February 23, 2012.

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## Share Repurchases

We repurchased 2,240,196 shares of our common stock during 2011 at a cost of \$120.9 million, including \$105.0 million in open market purchases at an average price of \$53.59 per share and \$15.9 million for the value of employees' stock-based compensation share awards surrendered to satisfy their personal statutory income tax withholding obligations. In 2010 and 2009, we repurchased 388,694 and 56,953 shares of our common stock, respectively, at a cost of \$19.0 million and \$0.8 million, respectively. See Part II, Item 2, Unregistered Sales of Equity Securities and Use of Proceeds. Under the current \$50 million authorization for 2012 share repurchases, the Company purchased 235,105 shares for \$16.1 million as of February 22, 2012.

## Debt Instruments and Related Covenants

Debt Instruments and Related Covenants (\$ in millions)	For the Years Ended December 31,		
	2011	2010	2009
Changes in short-term debt	\$2.3	\$3.3	\$(23.8)
Proceeds from issuances of long-term debt	226.7	48.2	33.5
Payments on long-term debt	(128.5)	(56.3)	(132.2)
Net proceeds from (payments on) borrowings	\$100.5	\$(4.8)	\$(122.5)

Net proceeds from long-term debt were \$98.2 million and net payments on short-term debt were \$2.3 million during 2011. With the current level of borrowing and forecasted results, we expect to remain in compliance with our Credit Agreement financial covenants.

In May 2011, the Company entered into a new unsecured revolving credit facility, or Credit Agreement, which replaced its former credit facility that was scheduled to expire in July 2012. The five-year revolving Credit Agreement provides for borrowing capacity of approximately \$225 million and includes a \$100 million equivalent sub-limit available in euro, as well as a \$25 million equivalent sub-limit available in Philippine pesos. Availability under the Credit Agreement was \$95.6 million as of December 31, 2011. We also had availability under our bank overdraft facilities and lines of credit of \$41.2 million as of December 31, 2011.

The Credit Agreement contains representations and warranties which are customary for facilities of this type and covenants and provisions that, among other things, require the Company to maintain (a) a Maximum Net Debt to EBITDA Ratio of 3.00 and (b) Minimum Interest Coverage of 3.50. The Company was in compliance with its financial covenants at December 31, 2011.

Our total debt to capital ratios at December 31, 2011 and December 31, 2010 were 23.5% and 9.0%, respectively.

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## Other Factors Affecting Liquidity and Capital Resources

The following table represents our future contractual cash requirements for the next five years and thereafter for our long-term debt obligations and other commitments (\$ in millions):

Contractual Obligations	Payments due for the years ended						
	Total	2012	2013	2014	2015	2016	Thereafter
Current debt <sup>(1)</sup>	\$5.0	\$5.0	\$—	\$—	\$—	\$—	\$—
Long-term debt <sup>(2)</sup>	141.0	—	2.2	2.8	3.1	132.9	—
Debt interest <sup>(3)</sup>	12.8	3.0	3.0	2.9	2.8	1.1	—
Restructuring obligations <sup>(4)</sup>	12.9	5.8	1.6	2.1	1.8	1.1	0.5
Minimum operating lease payments <sup>(5)</sup>	9.3	0.9	1.2	1.3	1.2	1.2	3.5
Purchase obligations - raw materials <sup>(6)</sup>	48.3	42.8	3.3	2.2	—	—	—
Purchase obligations - energy <sup>(7)</sup>	88.1	40.5	8.7	8.7	8.7	3.9	17.6
Purchase obligations - capital projects	2.9	2.9	—	—	—	—	—
Other long-term liabilities <sup>(8) (9) (10)</sup>	—	—	—	—	—	—	—
Total	\$320.3	\$100.9	\$20.0	\$20.0	\$17.6	\$140.2	\$21.6

(1) Current debt includes borrowings against bank overdraft facilities; see Note 10, Debt, of the Notes to Consolidated Financial Statements.

(2) See additional information regarding long-term debt in Note 10, Debt, of the Notes to Consolidated Financial Statements.

(3) The amounts reflected in debt interest are based upon the short-term and long-term scheduled principal maturities and interest rates in effect as of December 31, 2011. Where specific maturities are not stated, such as for an overdraft line-of-credit, a repayment date coinciding with the end of the year was used for purposes of these calculations. Since our debt is largely variable interest rate debt, applicable market interest rates were assumed to be the same as at December 31, 2011 for purposes of these calculations. With respect to our variable-rate debt outstanding at December 31, 2011, a 100 basis point increase in interest rates would increase our debt interest obligation by \$0.4 million in 2012. For more information regarding our outstanding debt and associated interest rates, see Note 10, Debt, of the Notes to Consolidated Financial Statements.

(4) Restructuring obligations are more fully discussed in Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operation, Recent Developments and Note 9, Restructuring and Impairment Activities, of the Notes to Consolidated Financial Statements.

(5) Minimum operating lease payments relate to our future minimum obligations under non-cancelable operating leases having an initial or remaining term in excess of one year as of December 31, 2011.

(6) Purchase obligations for raw materials include our calcium carbonate purchase agreement at our mill in Quimperlè, France, in which a vendor operates an on-site calcium carbonate plant and our mill has minimum purchase quantities. See Note 16, Commitments and Contingencies, of the Notes to Consolidated Financial Statements for additional information.

(7)

Purchase obligations for energy include obligations under agreements with (1) an energy cogeneration supplier at our mills in Quimperlè and Spay, France, to supply steam and our mills have minimum purchase commitments (2) a natural gas supplier to supply and distribute 100% of the natural gas needs of our Quimperlè mill and (3) an energy supplier to supply a constant supply of electricity for our Pirahy mill in Brazil. See Note 16, Commitments and Contingencies, of the Notes to Consolidated Financial Statements for additional information.

(8) We had no other long-term liabilities as defined for purposes of this disclosure by the SEC as of December 31, 2011.

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The amounts reflected in other long-term liabilities do not include any amounts for our pension obligations. The pension obligations are funded by our separate pension trusts, which held \$124.1 million in assets at December 31, 2011. The combined projected benefit obligation, or PBO, of our U.S. and French pension plans was underfunded by \$30.8 million and \$32.6 million as of December 31, 2011 and 2010, respectively. We make contributions to our (9) pension trusts based on many factors including regulatory guidelines, investment returns of the trusts and availability of cash for pension contributions versus other priorities. We were not required to make contributions to our U.S. and French pension plans during 2012. We expect 2012 funding to be in compliance with the Pension Protection Act of 2006. For information regarding our long-term pension obligations and trust assets, see Note 14, Postretirement and Other Benefits, of the Notes to Consolidated Financial Statements.

The amounts reflected in other long-term liabilities do not include any amounts for our postretirement healthcare and life insurance benefits. Such payments are dependent upon the incurrence of costs and filing of claims by our retirees and thus the amounts of such future payments are uncertain. Our net payments under these plans were (10) approximately \$1 million in both of the years ended December 31, 2011 and 2010. Based on this past experience, we currently expect our share of the net payments to be approximately \$1 million during 2012 for these benefits. For more information regarding our retiree healthcare and life insurance benefit obligations, see Note 14, Postretirement and Other Benefits, of the Notes to Consolidated Financial Statements.

## Outlook

With the anticipated adoption of LIP legislation in additional countries in coming years, SWM is poised to leverage its strong market position in this premium application and continue to improve the margin profile of its core paper business.

The Company is also set to further capitalize on Asian growth opportunities and regulatory trends requiring more sophisticated cigarettes in design and performance. As tar delivery limits are implemented in China, SWM expects increased demand for reconstituted tobacco leaf, which we are strategically positioned to satisfy.

We have built a rock-solid foundation with great opportunities ahead. The 2012 year may be challenging because of the global economy, continued decline of cigarette consumption in western markets and foreign exchange volatility. SWM expects to continue driving cost reductions through our operational excellence and lean manufacturing efforts. These cost reductions coupled with greater efficiencies as our European LIP capacity matures, are expected to deliver value to our customers and to mitigate anticipated inflationary impacts.

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### Forward-Looking Statements

This report contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 that are subject to the safe harbor created by that Act. These statements include those in the “Outlook” section and our expectations elsewhere in Management's Discussion and Analysis of Financial Condition and Results of Operation, and in “Risk Factors” in Item 1A. They also include statements containing “expect,” “anticipate,” “project,” “appears,” “should,” “could,” “may,” “typically” and similar words. Actual results may differ materially from the results suggested by these statements for a number of reasons, including the following:

SWM has manufacturing facilities in 7 countries, two joint ventures in China, and sells products in over 90 countries. As a result, it is subject to a variety of import and export tax, foreign currency, labor and other regulations within these countries. Changes in these regulations, adverse interpretations or applications, as well as changes in currency exchange rates, could adversely impact the Company's business in a variety of ways, including increasing expenses, decreasing sales, limiting its ability to repatriate funds and generally limiting its ability to conduct business.

The Company's sales are concentrated to a limited number of customers. In 2011, 54% of its sales were to its four largest customers. The loss of one or more of these customers, or a significant reduction in one or more of these customers' purchases, particularly those that impact our higher value LIP papers or reconstituted tobacco, could have a material effect on the Company's results of operations.

The Company's financial performance is materially impacted by sales of both reconstituted tobacco products and cigarette paper for lower ignition propensity cigarettes. A significant change in sales or production volumes, pricing or manufacturing costs of these products could have a material impact on future financial results. In this regard, Philip Morris-USA began advising the Company in 2009 that it disputes the manner in which the Company has calculated costs for banded cigarette papers under a cost-plus based contract for this product during the period April 2009 through December 2010. Notwithstanding that the dispute is now over a year old, and SWM has consistently advised Philip Morris-USA that it disagrees with its position, Philip Morris-USA to-date has not instituted any formal action to bring this matter to a close. Philip Morris-USA has also consistently paid the full invoiced amount from the date of the first notice of dispute to the present thereby avoiding any contention by SWM that the agreement has been breached for non-payment. Philip Morris-USA's action reflects a requirement found in the Virginia Uniform Commercial Code, the law that governs the contract, that suggests a party making full payment of a disputed invoice potentially waives any right to recover the amount paid unless such payment is accompanied by an explicit reservation of rights. Currently, the disputed amount is approximately \$24.4 million. While the Company believes that it has properly calculated the amount it invoiced, the ultimate resolution of this dispute, if unfavorable to the Company, could have a material adverse effect on the Company's results of operations.

As a result of excess capacity in the tobacco-related papers industry and increased operating costs, competitive levels of selling prices for certain of the Company's products are not sufficient to cover those costs with a margin that the Company considers reasonable. Such competitive pressures have resulted in downtime of certain paper machines and, in some cases, accelerated depreciation or impairment charges for certain equipment as well as employee severance expenses associated with downsizing activities. The Company will continue to disclose any such actions as they are announced to affected employees or otherwise become certain and will continue to provide updates to any previously disclosed expectations of expenses associated with such actions.

The demand for our reconstituted tobacco leaf product is subject to change depending on the rate at which this product is included in the blend that forms the column of tobacco in various cigarette brands as well as the supply and cost of natural tobacco leaf, which serves to an extent as a substitute for reconstituted tobacco. A change in the inclusion rate or the dynamics of the natural leaf tobacco market can have a material effect on the volume of reconstituted tobacco sales, the price for reconstituted tobacco or both, either of which can have a material effect on

our earnings from that product line. In past years, the Company has experienced the adverse effects for one or more years related to changes in the demand and supply relationship for natural leaf.



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In recent years, governmental entities around the world, particularly in the United States and western Europe, have taken or have proposed actions that may have the effect of reducing consumption of tobacco products. Reports with respect to the possible harmful physical effects of cigarette smoking and use of tobacco products have been publicized for many years and, together with actions to restrict or prohibit advertising and promotion of cigarettes or other tobacco products, to limit smoking in public places and to increase taxes on such products, are intended to discourage the consumption of cigarettes and other such products. Also in recent years, certain governmental entities, particularly in North America, have enacted, considered or proposed actions that would require cigarettes to meet specifications aimed at reducing their likelihood of igniting fires when the cigarettes are not actively being smoked. Furthermore, it is not possible to predict what additional legislation or regulations relating to tobacco products will be enacted, or to what extent, if any, such legislation or regulations might affect our business.

Our portfolio of granted patents varies by country, which could have an impact on any competitive advantage provided by patents in individual markets. We rely on patent, trademark, and other intellectual property laws of the United States and other countries to protect our intellectual property rights. In order to maintain the benefits of our patents, we may be required to enforce certain of our patents against infringement through court actions. However, we may be unable to prevent third parties from using our intellectual property or infringing on our patents without our authorization, which may reduce any competitive advantage we have developed. If we have to litigate to protect these rights, any proceedings could be costly, time consuming, could divert management resources, and we may not prevail. We cannot guarantee that any United States or foreign patents, issued or pending, will continue to provide us with any competitive advantage or will not be successfully challenged by third parties. We do not believe that any of our products infringe the valid intellectual property rights of third parties. However, we may be unaware of intellectual property rights of others that may cover some of our products or services. In that event, we may be subject to significant claims for damages. Effectively policing our intellectual property and patents is time consuming and costly, and the steps taken by us may not prevent infringement of our intellectual property, patents or other proprietary rights in our products, technology and trademarks, particularly in foreign countries where in many instances the local laws or legal systems do not offer the same level of protection as in the United States.

- Recent uncertainty in the EU financial markets has increased the possibility of significant changes in foreign exchange rates as governments take counter measures. As a large portion of our commercial business is euro denominated, any material change in the euro to U.S. dollar exchange rate could impact our results on a consolidated basis.

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Item 7A. Quantitative and Qualitative Disclosures about Market Risk

Foreign Currency Risk

Changes in foreign currency exchange rates may have an impact on our operating profit. Since we transact business in many countries, some of our sale and purchase transactions are denominated in a currency other than the local currency of our operations. As a result, changes in exchange rates between the currencies in which the transaction is denominated versus the local currency of our operation into which the transaction is being recorded can impact the amount of local currency recorded for such transaction. This can result in more or less local currency revenue or cost related to such transaction and thus have an effect on our operating profit. Currency transaction risk is mitigated partially in France since some of the revenue and expense transactions of our French subsidiaries are denominated in U.S. dollars, providing a degree of natural hedging. Our Brazilian and Polish operations are more fully exposed to currency transaction risk, especially as a result of U.S. dollar and euro denominated sales, respectively.

Additionally, changes in foreign currency exchange rates may have an impact on the amount reported in other income (expense), net. Once the above-indicated receivables and payables from the sale and purchase transactions have been recorded, to the extent currency exchange rates change prior to settlement of the balance, a gain or loss on the non-local currency denominated asset or liability balance may be experienced, in which case such gain or loss is included in other income (expense), net.

We utilize forward and swap contracts and, to a lesser extent, option contracts to selectively hedge our exposure to foreign currency transaction risk when it is practical and economical to do so. The use of these contracts minimizes transactional exposure to exchange rate changes because the gains or losses incurred on the derivative instrument will offset, in whole or in part, the loss or gain on the underlying foreign currency exposure. These instruments are entered into with money center banks, insurance companies or government agencies, collectively known as counterparties. Usually, these contracts extend for no more than 12 months. We expect to continue to apply forward currency hedging in our Brazilian operations through 2014. As of December 31, 2011, a 10% unfavorable change in the exchange rate of our functional currencies and those of our subsidiaries against the prevailing market rates of non-local currencies involving our transactional exposures would have resulted in a net pre-tax loss of approximately \$2.9 million. These hypothetical gains or losses on foreign currency contracts and transactional exposures are defined as the difference between the contract rates and the hypothetical exchange rates. While we believe the above loss resulting from the hypothetical unfavorable changes in foreign currency exchange rates could be material to our results of operations, we reduce this risk by selectively hedging our exposure when it is practical and economical to do so.

Interest Rate Risk

We hold a combination of variable-rate and fixed-rate debt consisting of short-term and long-term instruments. We selectively hedge our exposure to interest rate increases on our variable-rate, long-term debt when it is practical and economical to do so. We utilize various forms of interest rate hedge agreements, including interest rate swap agreements and forward rate agreements. We utilize variable-to-fixed interest rate swap agreements, typically with contractual terms no longer than 24 months. Our strategy to manage exposure to interest rate changes did not change during 2011, and we do not expect any significant changes in our exposure to interest rate changes or in how such exposure is managed in the near future. Various outstanding interest-bearing instruments are sensitive to changes in interest rates. Interest rate changes would result in gains or losses in fair market value of fixed-rate debt due to differences between current market interest rates and the rates governing these instruments. With respect to our fixed-rate debt outstanding at December 31, 2011, a 10% change in interest rates would not result in a material change in the fair market value of such debt and with respect to our variable-rate debt outstanding at December 31, 2011, a 100 basis point increase in interest rates would result in a \$1.4 million impact to our future annual pre-tax earnings.



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Commodity Price Risk

We are subject to commodity price risks, the most significant of which relates to the price of wood pulp, which is our largest single component of raw material cost. The per ton cost of wood pulp is cyclical in nature and more volatile than general inflation. During the period from January 2009 through December 2011, the U.S. list price of northern bleached softwood kraft pulp, or NBSK, a representative pulp grade that we use, ranged from a low of \$635 per metric ton in April 2009 to a high of \$1,035 per metric ton in June 2011. We normally maintain approximately 30 to 60 days of inventories to support our operations. As a result, there is a lag in the impact of changes in the per ton list price of wood pulp on our cost of products sold. Selling prices of our paper products are influenced, in part, by the market price for wood pulp, which is determined by worldwide industry supply and demand. Generally, over time, we have been able to increase our selling prices in response to increased per ton wood pulp costs and have generally reduced our selling prices when wood pulp costs have significantly declined. Increases in prices of wood pulp could adversely impact our earnings if selling prices are not increased or if such increases do not fully compensate for or trail the increases in wood pulp prices. We have not utilized derivative instruments to manage this risk. With respect to our commodity price risk, a hypothetical 10% change in per ton wood pulp prices would impact our future annual pre-tax earnings by approximately \$7 million, assuming no compensating change in our selling prices. We believe that, while our exposure to commodity price risk is material to our results of operations, our customers understand such risk and over time changes in the price of wood pulp are typically reflected in selling prices.

Energy Supply and Cost Volatility

In France, Poland and in the United States, availability of energy is generally not expected to be an issue, although prices can fluctuate significantly based on variations in demand. In Brazil, where that country's production of electricity is heavily reliant upon hydroelectric plants, availability of electricity has been affected in the past by rain variations. Our Brazilian business currently has a sufficient supply of energy to continue its current level of operation.

Due to the competitive pricing in the markets for most of our products, we are typically unable to fully pass through higher energy costs to our customers. With respect to our purchased energy price risk, a hypothetical 10% change in per unit prices would impact our future annual pre-tax earnings by approximately \$9 million, assuming no compensating change in our selling prices.

Periodically, when we believe it is appropriate to do so, we enter into agreements to procure a portion of our energy for future periods in order to reduce the uncertainty of future energy costs. However, in recent years this has only marginally slowed the increase in energy costs due to the volatile changes in energy prices we have experienced.

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Schedules have been omitted because they are either not required, not applicable or the required information is included in the consolidated financial statements or notes thereto.

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## SCHWEITZER-MAUDUIT INTERNATIONAL, INC. AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF INCOME

(dollars in millions, except per share amounts)

	For the Years Ended December 31,			
	2011	2010	2009	
Net Sales	\$816.2	\$740.2	\$719.6	
Cost of products sold	575.7	543.6	531.8	
Gross Profit	240.5	196.6	187.8	
Selling expense	22.0	19.0	19.4	
Research expense	9.3	8.5	8.0	
General expense	60.1	46.1	47.3	
Total nonmanufacturing expenses	91.4	73.6	74.7	
Valuation allowance on ICMS business tax credits	15.9	—	—	
Restructuring and impairment expense	14.0	13.4	23.9	
Operating Profit	119.2	109.6	89.2	
Interest expense	2.6	1.8	4.3	
Other income (expense), net	(2.6	) 0.2	(1.1	)
Income from Continuing Operations before Income Taxes and	114.0	108.0	83.8	
Income from Equity Affiliates				
Provision for income taxes	31.1	39.8	25.3	
Income from equity affiliates	4.7	3.2	1.1	
Income from Continuing Operations	87.6	71.4	59.6	
Income (loss) from Discontinued Operations	5.0	(6.1	) (24.0	)
Net Income	\$92.6	\$65.3	\$35.6	
Net Income (Loss) per Share - Basic:				
Income per share from continuing operations	\$5.20	\$3.94	\$3.80	
Income (loss) per share from discontinued operations	0.30	(0.34	) (1.53	)
Net income per share – basic	\$5.50	\$3.60	\$2.27	
Net Income (Loss) per Share – Diluted:				
Income per share from continuing operations	\$5.16	\$3.86	\$3.69	
Income (loss) per share from discontinued operations	0.30	(0.33	) (1.49	)
Net income per share – diluted	\$5.46	\$3.53	\$2.20	
Weighted Average Shares Outstanding:				
Basic	16,615,100	17,686,700	15,550,100	
Diluted	16,743,400	18,049,400	16,003,500	

The accompanying notes are an integral part of these consolidated financial statements.



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SCHWEITZER-MAUDUIT INTERNATIONAL, INC. AND SUBSIDIARIES  
 CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME  
 (dollars in millions)

	For the Years Ended December 31,		
	2011	2010	2009
Net Income	\$92.6	\$65.3	\$35.6
Other Comprehensive Income, net of tax:			
Foreign currency translation adjustments	(17.6	) 0.2	24.8
Less: Reclassification adjustment for translation adjustments realized upon deconsolidation of foreign subsidiary	(1.0	) —	—
Unrealized gains on derivative instruments	0.6	7.5	9.8
Less: Reclassification adjustment for gains on derivative instruments included in net income	(5.5	) (8.0	) (3.0
Net gain (loss) from postretirement benefit plans	(1.1	) (3.7	) 10.6
Less: Amortization of postretirement benefit plans' costs included in net periodic benefit cost	(1.4	) (1.2	) (4.9
Other Comprehensive Income (Loss)	(26.0	) (5.2	) 37.3
Comprehensive Income	\$66.6	\$60.1	\$72.9

The accompanying notes are an integral part of these consolidated financial statements.



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SCHWEITZER-MAUDUIT INTERNATIONAL, INC. AND SUBSIDIARIES  
 CONSOLIDATED BALANCE SHEETS  
 (dollars in millions, except per share amounts)

	December 31, 2011	December 31, 2010
<b>ASSETS</b>		
Current Assets		
Cash and cash equivalents	\$76.5	\$87.3
Accounts receivable	112.3	98.9
Inventories	113.8	113.8
Income taxes receivable	2.9	0.9
Current deferred income tax benefits	18.2	6.2
Other current assets	3.3	5.7
Total Current Assets	327.0	312.8
Property, Plant and Equipment, net	428.8	440.8
Deferred Income Tax Benefits	11.8	11.8
Investment in Equity Affiliates	38.7	20.5
Goodwill and Intangible Assets	7.1	8.8
Other Assets	31.8	55.7
Total Assets	\$845.2	\$850.4
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current Liabilities		
Current debt	\$5.0	\$8.7
Accounts payable	53.7	66.4
Accrued expenses	82.1	111.6
Total Current Liabilities	140.8	186.7
Long-Term Debt	141.0	43.1
Pension and Other Postretirement Benefits	42.3	46.3
Deferred Income Tax Liabilities	19.8	28.9
Other Liabilities	25.4	21.2
Total Liabilities	369.3	326.2
Stockholders' Equity:		
Preferred stock, \$0.10 par value; 10,000,000 shares authorized; none issued or outstanding	—	—
Common stock, \$0.10 par value; 100,000,000 shares authorized; 18,793,649 and 18,721,474 shares issued at December 31, 2011 and 2010, respectively; 16,183,442 and 18,027,903 shares outstanding at December 31, 2011 and 2010, respectively	1.9	1.9
Additional paid-in-capital	211.7	208.8
Common stock in treasury, at cost, 2,610,207 and 693,571 shares at December 31, 2011 and 2010, respectively	(132.1	) (24.4
Retained earnings	418.9	336.4
Accumulated other comprehensive (loss) income, net of tax	(24.5	) 1.5
Total Stockholders' Equity	475.9	524.2

Total Liabilities and Stockholders' Equity	\$845.2	\$850.4
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The accompanying notes are an integral part of these consolidated financial statements.

SCHWEITZER-MAUDUIT INTERNATIONAL, INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY  
(dollars in millions, except per share amounts)

	Common Stock Issued			Treasury Stock		Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
	Shares	Amount	Additional Paid-In Capital	Shares	Amount			
Balance, December 31, 2008	16,078,733	\$1.6	\$ 64.6	748,953	\$(14.1 )	\$255.9	\$ (30.6 )	\$277.4
Net income						35.6		35.6
Other comprehensive income (loss), net of tax							37.3	37.3
Issuance of common stock	2,070,000	0.2	117.2					117.4
Dividends declared (\$0.60 per share)						(9.6 )		(9.6 )
Restricted stock issuances, net			(0.2 )	(13,500 )	0.2			—
Stock-based employee compensation expense			8.2					8.2
Excess tax benefits of stock-based employee compensation			3.3					3.3
Stock issued to directors as compensation	890			(3,306 )	0.1			0.1
Issuance of shares for options exercised	483,612	0.1	12.6	(30,750 )	0.6			13.3
Purchases of treasury stock				56,953	(0.8 )			(0.8 )
Balance, December 31, 2009	18,633,235	\$1.9	\$ 205.7	758,350	\$(14.0 )	\$281.9	\$ 6.7	\$482.2
Net income						65.3		65.3
Other comprehensive income (loss), net of tax							(5.2 )	(5.2 )
Dividends declared (\$0.60 per share)						(10.8 )		(10.8 )
Restricted stock issuances, net			(8.6 )	(453,473 )	8.6			—
Stock-based employee compensation expense			7.7					7.7
Excess tax benefits of stock-based employee compensation			1.6					1.6
Stock issued to directors as compensation	2,453		0.2					0.2
Issuance of shares for options exercised	85,786		2.2					2.2
Purchases of treasury stock				388,694	(19.0 )			(19.0 )
Balance, December 31, 2010	18,721,474	\$1.9	\$ 208.8	693,571	\$(24.4 )	\$336.4	\$ 1.5	\$524.2
Net income						92.6		92.6

Other comprehensive income (loss), net of tax								(26.0 )	(26.0 )
Dividends declared (\$0.60 per share)								(10.1 )	(10.1 )
Restricted stock issuances, net		(13.2 )	(323,560 )	13.2					—
Stock-based employee compensation expense		3.8							3.8
Excess tax benefits of stock-based employee compensation		10.0							10.0
Stock issued to directors as compensation	2,138	0.1							0.1
Issuance of shares for options exercised	70,037	2.2	—						2.2
Purchases of treasury stock				2,240,196	(120.9 )				(120.9 )
Balance, December 31, 2011	18,793,649	\$1.9	\$ 211.7	2,610,207	\$(132.1)	\$418.9	\$ (24.5 )		\$475.9

The accompanying notes are an integral part of these consolidated financial statements.

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SCHWEITZER-MAUDUIT INTERNATIONAL, INC. AND SUBSIDIARIES  
 CONSOLIDATED STATEMENTS OF CASH FLOW  
 (dollars in millions)

	For the Years Ended December 31,		
	2011	2010	2009
<b>Operations</b>			
Net income	\$92.6	\$65.3	\$35.6
Less: Income (loss) from discontinued operations	5.0	(6.1	) (24.0
Income from continuing operations	87.6	71.4	59.6
<b>Non-cash items included in net income:</b>			
Depreciation and amortization	43.6	40.0	43.9
Restructuring-related impairment	6.8	4.5	12.1
Valuation allowance on ICMS business tax credits	15.9	—	—
Amortization of deferred revenue	(6.0	) (7.2	) (5.1
Deferred income tax provision (benefit)	(15.9	) 25.4	22.0
Pension and other postretirement benefits	(6.5	) 2.1	(20.6
Stock-based compensation	3.8	7.7	8.2
Income from equity affiliates	(4.7	) (3.2	) (1.1
Excess tax benefits of stock-based awards	(10.0	) (1.6	) (3.3
Other items	(2.9	) (3.4	) 1.2
<b>Changes in operating working capital</b>			
Accounts receivable	(25.8	) (15.8	) 1.8
Inventories	(4.5	) 9.9	(10.2
Prepaid expenses	0.5	(0.1	) 1.2
Accounts payable	(4.5	) 17.4	(17.9
Accrued expenses	2.1	(5.5	) 10.6
Accrued incomes taxes	8.2	22.4	(24.9
Net changes in operating working capital	(24.0	) 28.3	(39.4
<b>Net cash provided (used) by operating activities of:</b>			
- Continuing operations	87.7	164.0	77.5
- Discontinued operations	(6.2	) (22.9	) (14.1
Cash Provided by Operations	81.5	141.1	63.4
<b>Investing</b>			
Capital spending	(60.9	) (73.7	) (15.3
Capitalized software costs	(1.3	) (9.3	) (5.5
Investment in equity affiliates	(12.2	) —	—
Other investing	2.3	1.8	0.6
Cash Used for Investing	(72.1	) (81.2	) (20.2
<b>Financing</b>			
Cash dividends paid to SWM stockholders	(10.1	) (10.8	) (9.6
Changes in short-term debt	2.3	3.3	(23.8
Proceeds from issuances of long-term debt	226.7	48.2	33.5
Payments on long-term debt	(128.5	) (56.3	) (132.2
Net proceeds from issuances of common stock	—	—	117.4
Purchases of treasury stock	(120.9	) (19.0	) (0.8
Proceeds from exercise of stock options	2.2	2.2	13.3

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Excess tax benefits of stock-based awards	10.0	1.6	3.3
Cash Provided by (Used in) Financing	(18.3	) (30.8	) 1.1
Effect of Exchange Rate Changes on Cash	(1.9	) 1.3	0.7
Increase (Decrease) in Cash and Cash Equivalents	(10.8	) 30.4	45.0
Cash and Cash Equivalents at beginning of period	87.3	56.9	11.9
Cash and Cash Equivalents at end of period	\$76.5	\$87.3	\$56.9

The accompanying notes are an integral part of these consolidated financial statements.

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### Note 1. General

#### Nature of Business

Schweitzer-Mauduit International, Inc., or SWM or the Company, is a multinational diversified producer of premium specialty papers headquartered in the United States of America. The Company manufactures and sells paper and reconstituted tobacco products to the tobacco industry as well as specialized paper products for use in other applications. The Company's tobacco-related products include cigarette, plug wrap and base tipping papers, or Cigarette Papers, used to wrap various parts of a cigarette, reconstituted tobacco leaf, or RTL, which is used as a blend with virgin tobacco in cigarettes and reconstituted tobacco wrappers and binders for machine-made cigars. These products are sold directly to the major tobacco companies or their designated converters in the Americas, Europe, Asia and elsewhere. Non-tobacco industry products are a diverse mix of products, certain of which represent commodity paper grades produced to maximize machine operations.

The Company is a manufacturer of high porosity papers, which are used in manufacturing ventilated cigarettes, banded and print banded papers for the production of lower ignition propensity, or LIP, cigarettes and the leading independent producer of RTL used in producing blended cigarettes. The Company conducts business in over 90 countries and currently operates 11 production locations worldwide, with mills in the United States, France, the Philippines, Indonesia, Brazil and Poland. The Company also has a 50% equity interest in two joint ventures in China.

As used in this 2011 Annual Report on Form 10-K, unless the context indicates otherwise, references to "we," "us," "our," "SWM," "Schweitzer-Mauduit" or similar terms include Schweitzer-Mauduit International, Inc. and its consolidated subsidiaries.

### Note 2. Summary of Significant Accounting Policies

#### Basis of Presentation

The accompanying consolidated financial statements and the notes thereto have been prepared in accordance with accounting principles generally accepted in the United States of America, or U.S. GAAP. The preparation of financial statements in conformity with U.S. GAAP requires the Company to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenue and expenses during the reporting periods. The Company believes the estimates and assumptions used in the preparation of these consolidated financial statements are reasonable, based upon currently available facts and known circumstances. Actual results may differ from those estimates and assumptions as a result of a number of factors, including those discussed elsewhere in this report and in its other public filings from time to time.

#### Reclassifications

In the Operations section of the Consolidated Statements of Cash Flow for the years ended December 31, 2010 and 2009, excess tax benefits of stock-based awards of \$1.6 million and \$3.3 million, respectively, have been reclassified to a separate new line item from changes in Accrued Income Taxes to conform to the current year financial statement presentation. On the Consolidated Balance Sheets, Deferred Revenue has been reclassified to Accrued Expenses to conform to current year financial statement presentation.

#### Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its wholly-owned, majority-owned and controlled subsidiaries. All intercompany balances and transactions have been eliminated. The Company did not have any special purpose entities during 2011, 2010 or 2009.

The Company's has two joint ventures with China National Tobacco Corporation, or CNTC. CNTC is the principal operating Company under China's State Tobacco Monopoly Administration. CNTC and our subsidiary, SM-China, each own 50% of the joint ventures. The paper joint venture China Tobacco Mauduit (Jiangmen) Paper Industry Co. LTD, or CTM, produces tobacco-related papers in China. The second joint venture China Tobacco Schweitzer (Yunnan) Reconstituted Tobacco Co. LTD., or CTS, will produce reconstituted tobacco leaf products. The Company uses the equity method to account for both joint ventures. Investment in equity affiliates represents the Company's investment in its China joint ventures. The Company's 50% share of the net income is included in the consolidated statements of income as income from equity affiliates.



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### Revenue Recognition

The Company recognizes revenue and the related accounts receivable when the following four criteria are met: (1) persuasive evidence of an arrangement exists; (2) ownership has transferred to the customer; (3) the selling price is fixed or determinable; and (4) collection is reasonably assured based on the Company's judgment regarding the collectability of its accounts receivable. Generally, the Company recognizes revenue when it ships its manufactured product and title and risk of loss passes to its customer in accordance with the terms of sale of the product. Revenue is recorded at the time of shipment for terms designated f.o.b., or free on board, shipping point. For sales transactions designated f.o.b. destination, revenue is recorded when the product is delivered to the customer's delivery site, at which time title and risk of loss are transferred. Provisions for discounts, returns, allowances, customer rebates and other adjustments are provided for in the same period the related revenue is recorded. Deferred revenue represents advance payments from customers which are earned based upon a mutually agreed-upon amount per unit of future product sales.

### Freight Costs

The cost of delivering finished goods to the Company's customers is recorded as a component of cost of products sold. Those costs include the amounts paid to a third party to deliver the finished goods. Any freight costs billed to and paid by a customer are included in revenue.

### Royalty Income

Royalties from non-exclusive, third-party patent licenses are recognized when earned, including monies received at an agreement's initiation attributable to past sales. The Company recognizes up-front payments upon receipt when it has no future performance requirement or ongoing obligation arising from its agreements and the payment is for a separate earnings process. Minimum annual royalties received in advance are deferred and are recognized in the period earned. The Company recognized \$17.0 million of royalty income during 2011.

### Foreign Currency Translation

The income statements of foreign entities are translated into U.S. dollars at average exchange rates prevailing during the periods presented. The balance sheets of these entities are translated at period-end exchange rates, and the differences from historical exchange rates are reflected in a separate component of accumulated other comprehensive income (loss) as unrealized foreign currency translation adjustments.

Foreign currency risks arise from transactions and balances denominated in non-local currencies. Losses resulting from remeasurement and settlement of such transactions and balances, included in other income (expense), net, were \$1.6 million, \$0.9 million and \$1.9 million in 2011, 2010 and 2009, respectively.

### Derivative Instruments

The Company is exposed to changes in foreign currency exchange rates, interest rates and commodity prices. The Company utilizes a variety of practices to manage these market risks, including where considered appropriate, derivative instruments. The Company uses derivative instruments only for risk management purposes and not for trading or speculation. All derivative instruments the Company uses are either exchange traded or are entered into with major financial institutions in order to reduce credit risk and risk of nonperformance by third parties. As of December 31, 2011, the Company had \$33.0 million of its variable-rate long-term debt fixed under interest rate swap agreements. Usually the contracts extend for no more than 12 months, although their contractual term has been as long as 24 months. The Company believes the credit risks with respect to the counterparties, and the foreign currency risks

that would not be hedged if the counterparties fail to fulfill their obligations under the contracts, are not material in view of its understanding of the financial strength of the counterparties.

Gains and losses on instruments that hedge firm commitments are deferred and included in the basis of the underlying hedged items. All other hedging gains and losses are included in period income or expense based on the period-end market price of the instrument. See Note 11. Derivatives, for more information.

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### Cash and Cash Equivalents

The Company considers all highly liquid, unrestricted investments with remaining maturities of three months or less to be cash equivalents, including money market funds with no restrictions on withdrawals.

### Impairment of Long-Lived Assets, Goodwill and Intangible Assets

The Company evaluates the carrying value of long-lived assets, including property and equipment, and goodwill when events and circumstances warrant a review. Goodwill is also tested for impairment annually during the fourth quarter. Goodwill may be evaluated using a qualitative evaluation and/or a two-step test at the reporting unit level. The first step compares the book value of the reporting unit to its fair value. If the book value of a reporting unit exceeds its fair value, we perform the second step. In the second step, we determine an implied fair value of the reporting unit's goodwill by allocating the fair value of the reporting unit to all of the assets and liabilities other than goodwill. The difference between the total fair value of the reporting unit and the fair value of all the assets and liabilities other than goodwill is the implied fair value of that goodwill. Any impairment loss is measured as the excess of the book value of the goodwill over the implied fair value of that goodwill. See Note 7. Goodwill and Intangible Assets for further discussion of the Company's annual impairment test results.

The carrying value of long-lived assets is reviewed each reporting period to determine if events or circumstances have changed which may indicate that the assets may be impaired or the useful life may need to be changed. The Company considers internal and external factors relating to each asset group, including expectation of future profitability, undiscounted cash flows and its plans with respect to the operations. If impairment is indicated, an impairment loss is measured by the amount the net carrying value of the asset exceeds its estimated fair value.

### Environmental Spending

Environmental spending is capitalized if such spending qualifies as property, plant and equipment, substantially increases the economic value or extends the useful life of an asset. All other such spending is expensed as incurred, including fines and penalties incurred in connection with environmental violations. Environmental spending relating to an existing condition caused by past operations is expensed. Liabilities are accrued when environmental assessments are probable and the costs can be reasonably estimated. Generally, timing of these accruals coincides with completion of a feasibility study or commitment to a formal plan of action.

### Capitalized Software Costs

The Company capitalizes certain purchases of software and software development costs in connection with major projects of software development for internal use. These costs are included in other assets on the consolidated balance sheets and are amortized using the straight-line method over the estimated useful life not to exceed seven years. Costs associated with business process redesign, end-user training, system start-up and ongoing software maintenance are expensed as incurred. Amortization of capitalized software was \$6.8 million, \$5.3 million and \$4.7 million for the years ended December 31, 2011, 2010 and 2009, respectively. Accumulated amortization of capitalized software costs was \$49.6 million and \$44.2 million at December 31, 2011 and 2010, respectively.

### Business Tax Credits

Business tax credits represent value added tax credits receivable and similar assets, such as Imposto sobre Circulação de Mercadorias e Serviços, or ICMS, in Brazil. Business tax credits are generated when value-added taxes, or VAT, are paid on purchases. VAT and similar taxes are collected from customers on certain sales. In some jurisdictions, export sales do not require VAT collection. See Note 8. Other Assets for more information.

## Income Taxes

The Company uses an asset and liability approach to account for and report income taxes. Deferred income tax assets and liabilities are computed annually for differences between the financial statement and tax bases of assets and liabilities that will result in taxable or deductible amounts in the future based on enacted tax laws and rates applicable to the periods in which the differences are expected to affect taxable income. Income tax expense (benefit) is the tax payable or refundable for the period plus or minus the change during the period in deferred tax assets and liabilities. Valuation allowances are recognized to reduce deferred tax assets to the amount that is more likely than not to be realized. In assessing the likelihood of realization, the Company considers sources of future taxable income.

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In connection with income tax assessments or unrecognized tax benefits, the Company classifies penalties as provision for income taxes and interest as interest expense in its consolidated statements of income.

The Company files income tax returns in the U.S. Federal and several state jurisdictions as well as in many foreign jurisdictions. In France, the Company reorganized its legal entities to maximize utilization of its net operating loss carryforwards. With certain exceptions, the Company is no longer subject to U.S. Federal, state and local, or foreign income tax examinations for years before 2008.

**Pension and Other Postretirement Benefits Accounting**

The Company recognizes the estimated compensation cost of employees' pension and other postretirement benefits over their approximate period of service. The Company's earnings are impacted by amounts of expense recorded related to these benefits, which primarily consist of U.S. and French pension benefits and U.S. other postretirement benefits, or OPEBs. Each year's recorded expenses are estimates based on actuarial calculations of the Company's accumulated and projected benefit obligations, or PBOs, for the Company's various plans.

Suspension of additional benefits for future service is considered a curtailment, and if material, necessitates a remeasurement of plan assets and PBO. As part of a remeasurement, the Company adjusts its discount rates and other actuarial assumptions, such as retirement, turnover and mortality table assumptions, as appropriate.

**Comprehensive Income (Loss)**

Comprehensive income (loss) includes net income, as well as items charged and credited directly to stockholders' equity, which are excluded from net income. The Company has presented comprehensive income (loss) in the consolidated statements of comprehensive income.

Components of accumulated other comprehensive income were as follows (\$ in millions):

	December 31,	
	2011	2010
Accumulated pension and OPEB liability adjustments, net of income tax of \$24.8 million and \$25.3 million at December 31, 2011 and 2010, respectively	\$(44.2 )	\$(41.7 )
Accumulated unrealized gain on financial instruments, net of income tax of \$(0.6) million and \$2.0 million at December 31, 2011 and 2010, respectively	0.4	5.3
Accumulated unrealized foreign currency translation adjustments	19.3	37.9
Accumulated other comprehensive income	\$(24.5 )	\$1.5

Changes in the components of accumulated other comprehensive income (loss) were as follows (\$ in millions):

	For the Years Ended December 31,						2009		
	2011			2010			2009		
	Pre-tax	Tax	Net of Tax	Pre-tax	Tax	Net of Tax	Pre-tax	Tax	Net of Tax
Pension and OPEB liability adjustments	\$(2.0 )	\$(0.5 )	\$(2.5 )	\$(8.8 )	\$3.9	\$(4.9 )	\$9.3	\$(3.6 )	\$5.7
Unrealized gain (loss) on financial instruments	(7.5 )	2.6	(4.9 )	(0.9 )	0.4	(0.5 )	9.9	(3.1 )	6.8
Unrealized foreign currency translation adjustments	(18.6 )	—	(18.6 )	0.2	—	0.2	24.8	—	24.8
Total	\$(28.1 )	\$2.1	\$(26.0 )	\$(9.5 )	\$4.3	\$(5.2 )	\$44.0	\$(6.7 )	\$37.3



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### Treasury Stock

Common stock purchased for treasury is recorded at cost. At the date of subsequent reissue, the treasury stock account is reduced by the cost of such stock on the weighted-average cost basis.

### Employee Stock Options

The Company calculates stock option expense based on the grant date fair value. Stock options have not been granted since 2005 and are not expected to be utilized by the Company in the future. A summary of the status of stock options outstanding as of December 31, 2011 and changes during the three years then ended is presented in Note 15, Stockholders' Equity.

### Restricted Stock

The Company's restricted stock grants generally vest upon completion of a specified period of time. The fair value of each award is equal to the share price of the Company's stock on the date of the grant. This cost is recognized over the vesting period of the respective award. A summary of outstanding restricted stock awards as of December 31, 2011 and 2010 is included in Note 15. Stockholders' Equity.

### Restricted Stock Plan Performance Based Shares

The Company's Long-Term Incentive Plan, or LTIP, for key executives includes an equity-based award component that is provided through its Restricted Stock Plan, or RSP. The objectives under the LTIP are established for multiple years at the beginning of a performance cycle and are intended to focus management on longer-term strategic goals. The Compensation Committee of the Board of Directors designates participants in the LTIP and RSP and determines the equity-based award opportunity in the form of restricted stock for each performance cycle, which is generally measured on the basis of a two or three-year performance period. Performance is measured on a cumulative basis and a portion of each performance cycle's restricted stock award opportunity may be earned annually. The restricted shares are considered issued and outstanding when the number of shares becomes fixed, after the annual performance is determined, and such awards vest at the end of the performance cycle. The Company recognizes compensation expense with an offsetting credit to additional paid-in-capital over the performance period based on the fair value of the award at the date of grant, with compensation expense being adjusted cumulatively based on the number of shares expected to be earned according to the level of achievement of performance goals.

### Fair Value Option

The Company has elected not to measure its financial instruments or certain commitments at fair value.

### Recent Accounting Pronouncements

Effective December 31, 2011, the Company retrospectively adopted the requirements of ASC 220, Presentation of Comprehensive Income, which amends the presentation of comprehensive income. To adopt the guidance, the Company added a new financial statement Consolidated Statements of Comprehensive Income which immediately follows the Consolidated Statements of Income and presents the information on pension and OPEB liability adjustments, unrealized gain (loss) on financial instruments and unrealized foreign currency translation adjustments which were previously presented in the Consolidated Statements of Changes in Stockholders' Equity. In December 2011, an update to this guidance deferred the effective date for the presentation of reclassification of items out of accumulated other comprehensive income to some future period.





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## Note 3. Discontinued Operations

Due to ongoing losses, the Company decided in 2009 to close its Malaucène, France finished tipping paper mill. During 2010, the run off operations at our Malaucène, France mill were completed and, therefore operations at the Malaucène mill are reported as discontinued operations for all periods presented. Consequently, results of the Malaucène mill have been removed from each individual line within the statements of income and the operating activities section of the statements of cash flow. In each case a separate line has been added for the net results of the discontinued operation, including previously reported restructuring and impairment amounts.

The Malaucène mill filed for liquidation under applicable French law during the fourth quarter of 2011. As part of the liquidation process, a trustee was appointed to administer claims of the mill from the remaining assets of the entity. This appointment resulted in the Company's loss of control of the ability to direct the activities of Malaucène; therefore, the accounts of Malaucène have been removed from the consolidated results of the Company as of the liquidation date. The Company no longer has continuing involvement or an ongoing interest in Malaucène. The deconsolidation resulted in a \$5.7 million gain, presented in the results of discontinued operations, to remove the carrying value of Malaucène's assets and liabilities and a \$0.7 million tax benefit as a result of certain intercompany transaction losses which are deductible for French taxes.

Restructuring expense incurred during all periods presented primarily related to additional severances, claims from employees for additional severances and environmental remediation costs.

Included in the Consolidated Balance Sheets are the following major classes of assets and liabilities associated with the discontinued operations (\$ in millions):

	December 31,	
	2011	2010
Assets of discontinued operations:		
Current assets	\$—	\$3.9
Noncurrent deferred income tax benefits	—	8.0
Other assets – assets held for sale	—	0.4
Liabilities of discontinued operations:		
Current liabilities	—	12.2

Summary comparative financial results of discontinued operations were as follows (\$ in millions):

	For the Years Ended December 31,		
	2011	2010	2009
Net sales	\$—	\$0.6	\$20.8
Restructuring and impairment expense	1.5	7.9	26.3
Gain on deconsolidation	5.7	—	—
Income (loss) from discontinued operations before income taxes	3.6	(9.3	) (36.5
Income tax benefit	1.4	3.2	12.5
Income (loss) from discontinued operations	5.0	(6.1	) (24.0



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Restructuring liabilities related to discontinued operations were classified within accrued expenses in the December 31, 2010 consolidated balance sheet. Changes in the restructuring liabilities during 2011 and 2010 are summarized as follows (\$ in millions):

	2011	2010
Balance at beginning of year	\$9.2	\$20.9
Accruals for announced programs	1.2	7.7
Cash payments	(2.5	) (17.8
Exchange rate impacts	—	(1.6
Gain on deconsolidation	(7.9	) —
Balance at end of period	\$—	\$9.2

## Note 4. Accounts Receivable

Accounts receivable are summarized as follows (\$ in millions):

	December 31,	
	2011	2010
Trade receivables	\$85.5	\$70.7
Business tax credits, including VAT	6.1	13.3
Hedge contracts receivable	1.6	4.2
Other receivables	19.8	11.4
Less allowance for doubtful accounts and sales discounts	(0.7	) (0.7
Total accounts receivable	\$112.3	\$98.9

## Note 5. Inventories

Inventories are valued at the lower of cost using the First-In, First-Out, or FIFO, and weighted average methods, or market. The Company's inventorable costs primarily include pulp, chemicals, direct labor, utilities, maintenance, depreciation, finishing supplies and an allocation of mill overhead costs. Machine start-up costs or abnormal machine shut downs are expensed in the period incurred and are not inventoried. The definition of market value, with respect to all inventories, is replacement cost or net realizable value. The Company reviews inventories at least quarterly to determine the necessity of write-offs for excess, obsolete or unsalable inventory. The Company estimates reserves for inventory obsolescence and shrinkage based on its judgment of future realization. These reviews require the Company to assess customer and market demand. The following schedule details inventories by major class (\$ in millions):

	December 31,	
	2011	2010
Raw materials	\$27.7	\$31.7
Work in process	29.4	23.8
Finished goods	36.0	37.1
Supplies and other	20.7	21.2
Total	\$113.8	\$113.8

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## Note 6. Property, Plant and Equipment

Property, plant and equipment are stated at cost, less accumulated depreciation. Interest is capitalized as a component of the cost of construction for large projects. Expenditures for betterments are capitalized whereas normal repairs and maintenance are expensed as incurred. Property, other than land, is depreciated on the straight-line method for financial reporting purposes. When property is sold or retired, the cost of the property and the related accumulated depreciation are removed from the balance sheet, and any gain or loss on the transaction is normally included in cost of products sold.

Property, plant and equipment (and related depreciable lives) consisted of the following (\$ in millions):

	December 31,	
	2011	2010
Land and improvements	\$26.3	\$24.9
Buildings and improvements (20 to 40 years or remaining life of relevant lease)	154.4	137.0
Machinery and equipment (5 to 20 years)	669.5	680.8
Construction in progress	75.4	78.9
Gross Property	925.6	921.6
Less: Accumulated Depreciation	496.8	480.8
Property, Plant and Equipment, net	\$428.8	\$440.8

Depreciation expense was \$35.3 million, \$33.0 million and \$37.1 million for the years ended December 31, 2011, 2010 and 2009, respectively.

## Note 7. Goodwill and Intangible Assets

The Company evaluates goodwill for impairment as least annually during the fourth quarter. The annual tests during the fourth quarters of 2011 and 2009 resulted in no impairment. During the 2010 annual testing, the carrying value of goodwill related to Indonesia and Brazil, both part of the Paper segment, were found to exceed their respective implied fair values using a combination of market multiple and present value valuation methods. Country-specific risks, strengthening foreign currencies against the U.S. dollar and recent and projected operating performance were considered in the Company's determination of fair value. As a result, during 2010, the Company recorded impairment losses of \$2.7 million in the Paper segment. The 2010 impairments are also the cumulative goodwill impairments.

The changes in the carrying amount of goodwill for each segment were as follows (\$ in millions):

	Reconstituted Tobacco	Paper	Total
Goodwill as of January 1, 2010, net	\$6.3	\$2.7	\$9.0
Foreign currency translation adjustments	(0.5	) —	(0.5 )
Impairment losses	—	(2.7	) (2.7 )
Goodwill as of December 31, 2010	5.8	—	5.8
Foreign currency translation adjustments	(0.2	) —	(0.2 )
Goodwill as of December 31, 2011, gross	\$5.6	\$2.7	\$8.3
Accumulated impairment losses	—	(2.7	) (2.7 )
Goodwill as of December 31, 2011, net	\$5.6	\$—	\$5.6



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The gross carrying amount and accumulated amortization for amortizable intangible assets consisted of the following (\$ in millions):

	December 31, 2011			December 31, 2010		
	Gross Carrying Amount	Accumulated Amortization*	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization*	Net Carrying Amount
Customer-related intangibles (Reconstituted Tobacco Segment)	\$10.0	\$8.5	\$1.5	\$10.0	\$7.0	\$3.0

\* Accumulated amortization also includes adjustments for foreign currency translation.

Amortization expense of intangible assets was \$1.6 million, \$1.8 million and \$2.1 million for the years ended December 31, 2011, 2010 and 2009, respectively. The Company's customer-related intangibles are amortized to expense using the 150% declining balance method over a 6-year life. Estimated amortization expense is expected to be \$1.2 million and \$0.3 million during the years ended December 31, 2012 and 2013, respectively.

## Note 8. Other Assets

Other assets consisted of the following (\$ in millions):

	December 31	
	2011	2010
Capitalized software costs, net of accumulated amortization	\$17.2	\$23.2
Business tax credits, including VAT and ICMS (net of \$16.2 million reserve as of December 31, 2011)	3.9	18.9
Grantor trust assets	6.4	6.2
Other assets	4.3	7.4
Total	\$31.8	\$55.7

Business tax credits included \$14.8 million of Imposto sobre Circulação de Mercadorias e Serviços, or ICMS, tax credits as of December 31, 2010. The credits, which are a form of value-added tax in Brazil, are generated from the production and sale of certain non-tobacco related grades of paper sold in Brazil. During 2011, we received a special government action in the state of Rio de Janeiro to enable more rapid utilization of these credits. However, the action included certain limitations on the use of these credits for the paper industry and has a finite life of 48 months. As a result, utilization of the Company's credits may be delayed barring other changes outside of the Company's control. During 2011, the Company recorded a valuation allowance of \$16.2 million against the entire carrying value of its ICMS credits of which \$15.9 million is presented on the Consolidated Statements of Income in the line titled Valuation Allowance on ICMS Business Tax Credits and \$0.3 million is presented in Cost of Products Sold. These credits do not expire. The Company is still pursuing other actions to utilize the credits. Charges and credits associated with normal ongoing activity are included in Cost of Products Sold in the Consolidated Statements of Income. Future material changes as a result of new legislation or a change in our operations will be reported separately.

Grantor trust assets consist primarily of cash surrender values in Company-owned life insurance policies held by a trust to be used for the eventual payment of employee deferred compensation.

## Note 9. Restructuring and Impairment Activities

The Company incurred restructuring expenses of \$14.0 million, \$10.7 million and \$23.9 million in the years ended December 31, 2011, 2010 and 2009, respectively, in connection with previously announced restructuring activities. In 2010, the line item Restructuring and Impairment expense included \$2.7 million of Paper segment goodwill impairment.

In the Paper segment, rationalization of excess capacity in the base paper manufacturing footprint included restructuring actions to close the Lee Mills facilities in Lee, Massachusetts beginning in 2008, workforce reductions and shutting down a paper machine in Spotswood, New Jersey in 2009, workforce reductions and a small machine impairment in Quimperle, France in 2009 and a workforce reduction in Brazil in 2010.

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The Paper segment restructuring expense was \$9.4 million, \$10.5 million and \$22.8 million for the years ended December 31, 2011, 2010 and 2009, respectively, of which \$5.8 million, \$10.0 million and \$11.3 million was cash-related. In 2011, the Paper segment expense included \$3.6 million of non-cash fixed asset impairments, based on management's estimates of expected future cash flows, and \$5.3 million related to an early retirement plan offered to 40 French employees of PdM as part of the 2009 workforce reduction. The total cost of the plan, which is expected to be approximately \$9.0 million, will be recognized over the remaining required service period of the participants through 2014 and paid to participants through their respective normal retirement ages through 2017. In 2010, primarily all Paper segment restructuring expense was related to severances that were recorded over the remaining service periods of the affected employees. In 2009, the Paper segment restructuring and impairment expense included \$12.2 million for impairments of paper machines in Spotswood, New Jersey and Quimperle, France and \$10.8 million of restructuring expense related to severances that were recorded over the remaining service periods of the affected employees.

The Reconstituted Tobacco segment restructuring expense was \$4.6 million, \$0.2 million and \$1.1 million for the years ended December 31, 2011, 2010 and 2009, respectively, of which \$1.3 million, \$0.2 million and \$1.1 million was cash-related. In January 2011, the Company learned of decreased RTL needs of a major customer. As a consequence, management decided to suspend the construction of the RTL facility in the Philippines. In 2011, the Reconstituted Tobacco segment's restructuring and impairment expense included \$3.3 million impairment of RTL Philippines equipment requiring rework and \$1.3 million of expense related to severances and related suspension costs. The carrying value of the Philippine RTL facility was \$71.9 million as of December 31, 2011. In 2010 and 2009, the Reconstituted Tobacco segment's restructuring expense was related to severances that were recorded over the remaining service periods of the affected employees.

Restructuring liabilities were classified within accrued expenses in each of the consolidated balance sheets as of December 31, 2011 and December 31, 2010. Changes in the restructuring liabilities, substantially all of which are employee-related, during 2011 and 2010 are summarized as follows (\$ in millions):

	2011	2010
Balance at beginning of year	\$10.0	\$12.1
Accruals for announced programs	7.1	10.2
Cash payments	(9.5	) (11.2
Exchange rate impacts	(0.3	) (1.1
Balance at end of period	\$7.3	\$10.0



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## Note 10. Debt

Total debt is summarized in the following table (\$ in millions):

	December 31,	
	2011	2010
Revolving Credit Agreement	\$ 129.4	\$—
Euro Revolver	—	33.5
French Employee Profit Sharing	12.2	11.2
Bank Overdrafts	3.9	6.6
Other	0.5	0.5
Total Debt	146.0	51.8
Less: Current debt	(5.0	) (8.7
Long-Term Debt	\$ 141.0	\$ 43.1

## Credit Agreement

In May 2011, the Company entered into a new unsecured revolving credit facility, or Credit Agreement, which replaced its former credit facility executed on July 20, 2006 that was scheduled to expire in July 2012.

The five-year revolving Credit Agreement provides for borrowing capacity of approximately \$225 million with an option to increase borrowing capacity by \$100 million and includes a \$100 million equivalent sub-limit available in euro, of which €25 million was drawn at December 31, 2011, and a \$25 million equivalent sub-limit available in Philippine pesos. The Credit Agreement contains representations and warranties which are customary for facilities of this type and covenants and provisions that, among other things, require the Company to maintain (a) a Maximum Net Debt to EBITDA Ratio of 3.00 and (b) Minimum Interest Coverage of 3.50. The Company was in compliance with its financial covenants at December 31, 2011.

Under the Credit Agreement, interest rates are based on the London Interbank Offered Rate plus an applicable margin that varies from 1.25% to 2.00% depending on the Net Debt to EBITDA Ratio, as defined in the Credit Agreement. The Company will incur commitment fees at an annual rate of 0.20% to 0.30% of the applicable margin on the committed amounts not drawn, depending on the Net Debt to EBITDA Ratio. As of December 31, 2011, the applicable interest rate on Credit Agreement borrowings was 1.56% on US Dollar borrowings and 2.39% on euro borrowings.

## French Employee Profit Sharing

At both December 31, 2011 and 2010, long-term debt other than the Revolving Credit Agreement and Euro Revolver primarily consisted of obligations of the French operations related to government-mandated profit sharing. Each year, representatives of the workers at each of the French businesses can make an election for the profit sharing amounts from the most recent year ended to be invested in a financial institution or with their respective employer. To the extent that funds are invested with the Company, these amounts bear interest at 3.80% and 3.60% at December 31, 2011 and 2010, respectively, and are generally payable in the fifth year subsequent to the year the profit sharing is accrued.

## Bank Overdrafts and Other

The Company also had bank overdraft facilities of \$45.1 million and \$33.8 million, at December 31, 2011 and 2010, respectively, of which \$3.9 million and \$6.6 million were outstanding at December 31, 2011 and 2010, respectively,

and reported as current debt on the consolidated balance sheet. Interest is incurred on outstanding amounts at market rates and was 1.15% and 1.00%, respectively, at December 31, 2011 and 2010. No commitment fees are paid on the unused portion of these facilities.

Other debt consists of non-interest bearing French segment debt with deferred capital repayment from governmental and commercial institutions primarily related to environmental capital improvements.

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Interest Expense and Rate Swap Agreements

The Company capitalized \$1.5 million and \$0.7 million of interest expense in the years ended December 31, 2011 and 2010, respectively, due to construction of a RTL facility in the Philippines and the EU LIP facility in Poland.

The Company maintains interest rate swap agreements on portions of its long-term debt. As a result, as of December 31, 2011, the LIBOR rates on \$33.0 million of the Company's variable-rate long-term debt were fixed at 2.1%