SCHWEITZER MAUDUIT INTERNATIONAL INC
Form 10-Q
August 07, 2007

FORM 10-Q

FOR THE QUARTER ENDED JUNE 30, 2007

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2007

OR

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

For the transition period from to

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)

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

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

Large accelerated filer o Accelerated filer x Non-accelerated filer o

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

There were 15,708,817 shares of common stock, par value $0.10 per share, of the registrant outstanding as of August 3, 2007.

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* These Section 906 certifications are not being incorporated by reference into the Form 10-Q filing or otherwise deemed to be filed with the Securities and Exchange Commission.

PART I

ITEM 1. FINANCIAL STATEMENTS

SCHWEITZER-MAUDUIT INTERNATIONAL, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME

(dollars in millions, except per share amounts)

(Unaudited)

	Three Months Ended		Six Months Ended	
	June 30, 2007	**June 30, 2006**	**June 30, 2007**	**June 30, 2006**
Net Sales	$ 171.8	$ 162.1	$ 342.1	$ 327.5
Cost of products sold	145.8	139.9	287.8	280.7
Gross Profit	26.0	22.2	54.3	46.8
Selling expense	5.4	5.9	11.0	11.5
Research expense	2.0	1.9	4.0	3.7
General expense	9.2	6.8	18.1	14.5
Total nonmanufacturing expenses	16.6	14.6	33.1	29.7
Restructuring expense (see Note 4)	3.4	3.4	6.1	3.9
Operating Profit	6.0	4.2	15.1	13.2
Interest expense	1.5	1.4	2.8	2.8
Other expense, net	0.2	0.6	0.1	0.6
Income Before Income Taxes, Minority Interest and Loss from Equity Affiliates	4.3	2.2	12.2	9.8
Provision for income taxes	1.2	0.4	3.1	2.4
Minority interest in earnings of subsidiaries	2.1	1.0	3.8	2.0
Loss from equity affiliates		0.1	0.1	0.1
Net Income	$ 1.0	$ 0.7	$ 5.2	$ 5.3
Net Income Per Share:				
Basic	$ 0.06	$ 0.04	$ 0.33	$ 0.34
Diluted	$ 0.06	$ 0.04	$ 0.33	$ 0.34
Cash Dividends Declared Per Share	$ 0.15	$ 0.15	$ 0.30	$ 0.30
Weighted Average Shares Outstanding:				
Basic	15,605,300	15,399,600	15,551,500	15,377,100
Diluted	15,887,800	15,528,000	15,803,800	15,529,200

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

SCHWEITZER-MAUDUIT INTERNATIONAL, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(dollars in millions, except per share amounts)

(Unaudited)

	June 30, 2007	December 31, 2006 (1) (Restated)
ASSETS		
Current Assets		
Cash and cash equivalents	$ 8.5	$ 13.7
Accounts receivable	92.9	88.9
Inventories	128.1	119.2
Other current assets	12.8	14.3
Total Current Assets	242.3	236.1
Property, Plant and Equipment, net	426.8	416.8
Other Assets	56.9	44.2
Total Assets	$ 726.0	$ 697.1
LIABILITIES AND STOCKHOLDERS EQUITY		
Current Liabilities		
Current debt	$ 20.1	$ 17.1
Accounts payable	64.2	62.5
Accrued expenses	88.8	82.4
Current deferred revenue	6.0	6.0
Total Current Liabilities	179.1	168.0
Long-Term Debt	80.4	80.2
Pension and Other Postretirement Benefits	51.3	54.2
Deferred Income Tax Liabilities	27.9	29.0
Deferred Revenue	20.9	24.1
Other Liabilities	25.3	23.0
Total Liabilities	384.9	378.5
Minority Interest	19.9	15.6
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; 16,078,733 shares issued; 15,750,725 and 15,517,390 shares outstanding at June 30, 2007 and December 31, 2006, respectively	1.6	1.6
Additional paid-in-capital	63.7	63.3
Common stock in treasury, at cost, 328,008 and 561,343 shares atJune 30, 2007 and December 31, 2006, respectively	(6.7)	(11.4)
Retained earnings	271.1	270.6
Accumulated other comprehensive loss, net of tax	(8.5)	(21.1)
Total Stockholders Equity	321.2	303.0
Total Liabilities and Stockholders Equity	$ 726.0	$ 697.1

(1) - See Note 7, Prior Period Restatement

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 AND COMPREHENSIVE INCOME

(dollars in millions, except per share amounts)

(Unaudited)

	Common Stock Issued Shares	Common Stock Issued Amount	Additional Paid-In Capital	Treasury Stock Shares	Treasury Stock Amount	Retained Earnings	Unearned Compensation	Accumulated Other Comprehensive Income (Loss)	Total
Balance, December 31, 2005 (Restated) (1)	**16,078,733**	**$ 1.6**	**$ 63.8**	**770,977**	**$ (15.6)**	**$ 280.8**	**$ (0.3)**	**$ (38.4)**	**$ 291.9**
Net income for the six months ended June 30, 2006						5.3			5.3
Adjustments to unrealized foreign currency translation, net of tax								16.3	16.3
Comprehensive income, net of tax									21.6
Effect of adoption of SFAS No. 123R			(0.3)				0.3		
Dividends declared ($0.30 per share)						(4.7)			(4.7)
Restricted stock issuances, net			(0.4)	(24,000)	0.4				
Return of shares				13					
Stock-based compensation expense			0.2						0.2
Stock issued to directors as compensation				(3,020)	0.1				0.1
Excess tax benefits of stock-based awards			0.4						0.4
Issuance of shares for options exercised			(0.4)	(106,400)	2.2				1.8
Balance, June 30, 2006 (Restated) (1)	**16,078,733**	**$ 1.6**	**$ 63.3**	**637,570**	**$ (12.9)**	**$ 281.4**	**$**	**$ (22.1)**	**$ 311.3**
Balance, December 31, 2006 (Restated) (1)	**16,078,733**	**$ 1.6**	**$ 63.3**	**561,343**	**$ (11.4)**	**$ 270.6**	**$**	**$ (21.1)**	**$ 303.0**
Net income for the six months ended June 30, 2007						5.2			5.2
Adjustments to unrealized foreign currency translation, net of tax								11.8	11.8
Amortization of postretirement benefit plans actuarial losses and prior service costs,net of tax								0.8	0.8
Comprehensive income, net of tax									17.8
Dividends declared ($0.30 per share)						(4.7)			(4.7)
Restricted stock issuances, net			(0.6)	(29,960)	0.6				
Stock-based compensation expense			0.4						0.4
Stock issued to directors as compensation				(2,908)	0.1				0.1
Excess tax benefits of stock-based awards			0.3						0.3
Purchases of treasury stock				4,340	(0.1)				(0.1)
Issuance of shares for options exercised			0.3	(204,807)	4.1				4.4

Balance, June 30, 2007	**16,078,733**	**$**	**1.6**	**$**	**63.7**	**328,008**	**$**	**(6.7**	**) $**	**271.1**	**$**		**$**	**(8.5**	**) $**	**321.2**	

(1) See Note 7, Prior Period Restatement

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)

(Unaudited)

	Six Months Ended June 30, 2007	June 30, 2006
Operations		
Net income	$ 5.2	$ 5.3
Non-cash items included in net income		
Depreciation and amortization	19.4	19.2
Restructuring accelerated depreciation	1.5	3.1
Amortization of deferred revenue	(3.2)	(3.3)
Deferred income tax benefit	(4.0)	(2.9)
Minority interest in earnings of subsidiaries	3.8	2.0
Other items	0.3	1.4
Net changes in operating working capital	(1.1)	(2.6)
Cash Provided by Operations	21.9	22.2
Investing		
Capital spending	(18.3)	(2.1)
Capitalized software costs	(4.5)	(0.7)
Investment in equity affiliates	(6.5)	(2.5)
Other	(1.0)	(5.9)
Cash Used for Investing	(30.3)	(11.2)
Financing		
Cash dividends paid to SWM stockholders	(4.7)	(4.7)
Changes in short-term debt	2.4	(3.5)
Proceeds from issuances of long-term debt	13.0	21.2
Payments on long-term debt	(12.6)	(28.6)
Purchases of treasury stock	(0.1)	
Proceeds from exercise of stock options	4.4	1.8
Excess tax benefits of stock-based awards	0.3	0.4
Cash Provided by (Used for) Financing	2.7	(13.4)
Effect of Exchange Rate Changes on Cash	0.5	
Decrease in Cash and Cash Equivalents	(5.2)	(2.4)
Cash and Cash Equivalents at beginning of period	13.7	5.1
Cash and Cash Equivalents at end of period	$ 8.5	$ 2.7

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

NOTE 1. GENERAL

Nature of Business

Schweitzer-Mauduit International, Inc., or the Company, is a multinational diversified producer of premium specialty papers headquartered in the United States of America and is the world s largest supplier of fine papers to the tobacco industry. 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. Tobacco industry products comprised approximately 90 percent of the Company s consolidated net sales in each of the three and six months ended June 30, 2007 and 2006. The primary products in the group include cigarette, plug wrap and 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 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 the premier manufacturer of high porosity papers, which are used in manufacturing ventilated 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 and Brazil. The Company also has a 50 percent equity interest in a mill currently under construction in China.

During the second quarter of 2007, the Company acquired a production facility in South Carolina to be used for the processing of cigarette paper for lower ignition propensity, or LIP, cigarettes. The purchase price of the acquisition was $2.8 million. An initial estimate of the purchase price allocation is as follows: $2.0 million for the building, $0.6 million for the production equipment and $0.2 million for the land. Operations are expected to begin prior to year-end 2007.

Basis of Presentation

The accompanying unaudited consolidated financial statements and the notes thereto have been prepared in accordance with the instructions of Form 10-Q and Rule 10-01 of Regulation S-X of the Securities and Exchange Commission, or the SEC, and do not include all of the information and disclosures required by accounting principles generally accepted in the United States of America, or GAAP. However, such information reflects all adjustments (consisting of normal recurring adjustments) which are, in the opinion of management, necessary for a fair statement of results for the interim periods.

The results of operations for the three and six months ended June 30, 2007 are not necessarily indicative of the results to be expected for the full year. The unaudited consolidated financial statements included herein should be read in conjunction with the audited consolidated financial statements and the notes thereto included in the Company s Annual Report on Form 10-K for the year ended December 31, 2006 as filed with the SEC on March 2, 2007. The Company has restated its prior consolidated balance sheet for an immaterial adjustment originating in 2003, as described in Note 7, Prior Period Restatement.

Principles of Consolidation

The consolidated financial statements include the accounts of the Company and wholly-owned, controlled majority-owned and financially controlled subsidiaries. Minority interest represents minority stockholders proportionate share of the equity in LTR Industries S.A., or LTRI, and Schweitzer-Mauduit do Brasil S.A., or SWM-B. The Company s share of the net loss of its 50 percent owned joint venture in China is included in the consolidated statements of income as loss from equity affiliates. All significant intercompany balances and transactions have been eliminated.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires estimates and assumptions that affect the reported amounts of assets and liabilities, revenues and expenses and related disclosures of contingent assets and liabilities in the consolidated financial statements and accompanying notes. Estimates are used for, but not limited to, inventory valuation, depreciable lives, sales returns, receivables valuation, pension, postretirement and other benefits, restructuring, taxes and contingencies. Actual results could differ materially from those estimates.

Income Taxes

The Company adopted the provisions of Financial Accounting Standards Board, or FASB, Interpretation No. 48, or FIN 48, *Accounting for Uncertainty in Income Taxes* effective January 1, 2007. FIN 48 is an interpretation of Statement of Financial Accounting Standards, or SFAS, No. 109, *Accounting for Income Taxes*, which seeks to reduce the diversity in practice associated with certain aspects of measurement and recognition in accounting for income taxes. In addition, FIN 48 provides guidance on derecognition, classification, interest and penalties and accounting in interim periods and requires expanded disclosure with respect to the uncertainty in income taxes. Adoption of FIN 48 had no cumulative effect on the Company s consolidated financial position at January 1, 2007. At June 30, 2007, the Company had no significant unrecognized tax benefits related to income taxes.

The Company s policy with respect to penalties and interest in connection with income tax assessments or related to unrecognized tax benefits is to classify penalties as provision for income taxes and interest as interest expense in its consolidated income statement. There were no material income tax penalties or interest accrued during the six months ended June 30, 2007.

The Company files income tax returns in the U.S. Federal and several state jurisdictions as well as in many foreign jurisdictions. With certain exceptions, the Company is no longer subject to U.S. Federal, state and local, or foreign income tax examinations for years before 2003.

Credit Agreement Extension

On July 17, 2007, the Company and Schweitzer-Mauduit France S.A.R.L. received a 1-year extension under the current terms and conditions of its existing unsecured credit agreement. The credit agreement provided for a 5-year term with 2 1-year extension options, with the extensions at the discretion of the participating banks. The maturity date of the credit agreement was originally July 31, 2011 and has now been extended to July 31, 2012. All other provisions of the credit agreement remain unchanged.

Recent Accounting Pronouncements

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements,* which defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. SFAS No. 157 also expands disclosure requirements to include: (a) the fair value measurements of assets and liabilities at the reporting date, (b) segregation of assets and liabilities between fair value measurements based on quoted market prices and those based on other methods and (c) information that enables users to assess the method or methods used to estimate fair value when no quoted price exists. SFAS No. 157 is effective for financial statements issued for the fiscal year beginning after November 15, 2007. The Company is currently in the process of reviewing this guidance to determine its impact on the Company s consolidated financial position and results of operation and will implement SFAS No. 157 beginning January 1, 2008.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities,* which is effective as of the beginning of an entity s first fiscal year beginning after November 15, 2007. SFAS No. 159 permits entities to choose to measure many financial instruments and certain other items at fair value that are not currently required to be measured at fair value. A business entity shall report unrealized gains and losses on items for which the fair value option has been elected in earnings at each subsequent reporting date. Upfront costs and fees related to items for which the fair value option was elected shall be recognized in earnings as incurred and not deferred. The Company is currently in the process of analyzing this guidance to determine its impact on the Company s consolidated financial position and results of operation and will implement SFAS No. 159 beginning January 1, 2008.

NOTE 2. NET INCOME PER SHARE

Basic net income per common share is computed based on net income divided by the weighted average number of common shares outstanding. Diluted net income per common share is computed based on net income divided by the weighted average number of common and potential common shares outstanding. Potential common shares during the respective periods are those related to stock options outstanding, restricted stock outstanding, directors accumulated deferred stock compensation, which may be received by the directors in the form of stock or cash, and restricted stock estimated to be earned as part of the long-term incentive plan. A reconciliation of the average number of common and potential common shares outstanding used in the calculations of basic and diluted net income per share follows (in thousands):

	Three Months Ended		Six Months Ended	
	June 30, 2007	June 30, 2006	June 30, 2007	June 30, 2006
Average number of common shares outstanding	15,605.3	15,399.6	15,551.5	15,377.1
Dilutive effect of:				
stock options	79.6	60.3	69.6	86.5
restricted stock	103.6	38.9	102.0	39.0
directors deferred stock compensation	27.2	20.8	26.5	20.1
long-term incentive compensation	72.1	8.4	54.2	6.5
Average number of common and potential common shares outstanding	15,887.8	15,528.0	15,803.8	15,529.2

Certain stock options outstanding during the periods presented were not included in the calculations of diluted net income per share because the exercise prices of the options were greater than the average market prices of the common shares during the respective periods. The average number of share equivalents resulting from these anti-dilutive stock options not included in the computations of diluted net income per share for the three and six months ended June 30, 2007 were approximately 358,800 and 370,300, respectively, and for the three and six months ended June 30, 2006 were approximately 600,000 and 489,900, respectively.

NOTE 3. INVENTORIES

The following schedule details inventories by major class (dollars in millions):

	June 30, 2007	December 31, 2006
Raw materials	$ 37.7	$ 38.4
Work in process	21.2	19.1
Finished goods	49.3	42.3
Supplies and other	19.9	19.4
Total	$ 128.1	$ 119.2

NOTE 4. RESTRUCTURING ACTIVITIES

The Company initiated restructuring activities during 2006 which are expected to improve its competitiveness and profitability as well as address an imbalance between sales demand for its products and its paper production capacity in France and the United States. The Company recognized restructuring expense of $3.4 million and $6.1 million during the three and six months ended June 30, 2007, respectively, and $3.4 million and $3.9 million during the three and six months ended June 30, 2006, and $21.1 million during the full year of 2006.

The following table summarizes the associated cash and non-cash pretax restructuring expense in France and the United States for the three and six months ended June 30, 2007 and 2006 and the twelve months ended December 31, 2006 (dollars in millions):

	Three Months Ended June 30, 2007	June 30, 2006	Six Months Ended June 30, 2007	June 30, 2006	Twelve Months Ended December 31, 2006
France					
Cash Expense					
Severance and other employee related costs	$ 2.6	$ 0.1	$ 4.6	$ 0.1	$ 13.9
Other		0.1		0.1	0.9
Total cash expense	2.6	0.2	4.6	0.2	14.8
Non-cash Expense					
Accelerated depreciation	0.4	0.3	0.8	0.5	1.0
Other					
Total non-cash expense	0.4	0.3	0.8	0.5	1.0
Total France Restructuring Expense	$ 3.0	$ 0.5	$ 5.4	$ 0.7	$ 15.8
United States					
Cash Expense					
Severance and other employee related costs	$	$ 0.3	$	$ 0.3	$ 0.5
Other		0.2		0.2	0.1
Total cash expense		0.5		0.5	0.6
Non-cash Expense					
Accelerated depreciation	0.4	2.3	0.7	2.6	4.2
Other		0.1		0.1	0.5
Total non-cash expense	0.4	2.4	0.7	2.7	4.7
Total United States Restructuring Expense	$ 0.4	$ 2.9	$ 0.7	$ 3.2	$ 5.3
Summary					
Total Cash Expense	$ 2.6	$ 0.7	$ 4.6	$ 0.7	$ 15.4
Total Non-cash Expense	0.8	2.7	1.5	3.2	5.7
Total Restructuring Expense	$ 3.4	$ 3.4	$ 6.1	$ 3.9	$ 21.1

Restructuring liabilities were classified on each of the June 30, 2007 and December 31, 2006 consolidated balance sheets within accrued expenses. The activity during the six months ended June 30, 2007 and the twelve months ended December 31, 2006 is summarized as follows (dollars in millions):

	2007	2006
Balance at beginning of year	$ 13.9	$
Accruals for announced programs	4.6	15.4
Cash payments	(4.0)	(1.5)
Exchange rate impacts	0.4	
Balance at end of period	$ 14.9	$ 13.9

Restructuring costs are accounted for in accordance with SFAS No. 112, *Employers Accounting for Postretirement Benefits - An Amendment of FASB Statements No. 5 and 15,* SFAS No. 146, *Accounting for Costs Associated with Exit or Disposal Activities* and SFAS No. 88, *Employers Accounting for Settlements and Curtailments of Defined Benefit Pension Plans for Termination Benefits.* The actual amount of severance expense in France will be dependent upon the final number of individuals within each of the possible categories for employee severance that include early retirement, other voluntary terminations and involuntary layoffs, and which amount above the French legal minimum is being accrued and amortized to restructuring expense ratably over the affected employees remaining service periods.

NOTE 2. NET INCOME PER SHARE

NOTE 5. COMMITMENTS AND CONTINGENCIES

Litigation

The Company is involved in various legal proceedings and disputes (see Note 8, Commitments and Contingencies, of the Notes to the Consolidated Financial Statements in the Company s Annual Report on Form 10-K for the year ended December 31, 2006). There have been no material developments to these matters during 2007**,** except in the following case.

*Imposto sobre Produtos Industrializados***,** or IPI, a form of federal value-added tax in Brazil. Schweitzer-Mauduit do Brasil v. Federal Union, Federal Regional Tribunal sitting in Rio de Janeiro, case number 2004.51.04.000502-4 (March 5, 2004).

SWM-B instituted action in March 2004 to recover credits on past and future purchases of raw materials that are exempt from IPI taxes or that carry an IPI tax rate of zero, for which a favorable ruling was received at the first court level. The recovery would be in the form of presumed credits that could be applied to offset other IPI tax liabilities. The action for recovery is based on the principle in Brazilian law of non-cumulative taxes. The potential recovery of IPI credits, depending upon several contested factors, could be in the range of $10 million to $20 million, which amounts the Company considers a gain contingency and has not recorded in its consolidated financial statements. During March 2007, the Company received an unfavorable ruling on appeal before the Federal Tribunal. The final resolution of this matter will likely entail judicial proceedings up to and including presentation of the matter to the Supreme Court of Brazil and is not likely to be finally resolved for several years.

Environmental Matters

The Company s operations are subject to federal, state and local laws, regulations and ordinances relating to various environmental matters. The nature of the Company s operations exposes it to the risk of claims with respect to environmental matters, and there can be no assurance that material costs or liabilities will not be incurred in connection with such claims. While the Company has incurred in the past several years, and will continue to incur, capital and operating expenditures in order to comply with environmental laws and regulations, it believes that its future cost of compliance with environmental laws, regulations and ordinances, and its exposure to liability for environmental claims and its obligation to participate in the remediation and monitoring of certain hazardous waste disposal sites, will not have a material adverse effect on its financial condition or results of operations. However, future events, such as changes in existing laws and regulations, or unknown contamination of sites owned, operated or used for waste disposal by the Company (including contamination caused by prior owners and operators of such sites or other waste generators) may give rise to additional costs which could have a material adverse effect on its financial condition or results of operations.

NOTE 6. POSTRETIREMENT AND OTHER BENEFITS

The Company sponsors pension benefits in the United States, France, the Philippines and Canada and postretirement healthcare and life insurance, or OPEB, benefits in the United States and Canada. The Company s Canadian and Philippines pension and OPEB benefits are not significant and therefore are not included in the following disclosures.

U.S. Pension and OPEB Benefits

The components of net pension and OPEB benefit costs under U.S. plans for the three and six months ended June 30, 2007 and 2006 were as follows (dollars in millions):

U.S. Pension Benefits	**Three Months Ended**		**Six Months Ended**	
	June 30, 2007	**June 30, 2006**	**June 30, 2007**	**June 30, 2006**
Service cost	$ 0.2	$ 0.3	$ 0.5	$ 0.9
Interest cost	1.7	1.8	3.3	3.3
Expected return on plan assets	(1.9)	(1.7)	(3.8)	(3.5)
Amortization and other	0.6	0.6	1.1	1.3
Pension curtailment gain		(0.1)		(0.1)
Net periodic benefit cost	$ 0.6	$ 0.9	$ 1.1	$ 1.9

U.S. OPEB Benefits	**Three Months Ended**		**Six Months Ended**	
	June 30, 2007	**June 30, 2006**	**June 30, 2007**	**June 30, 2006**
Service cost	$	$	$ 0.1	$ 0.1
Interest cost	0.2	0.2	0.4	0.4
Net periodic benefit cost	$ 0.2	$ 0.2	$ 0.5	$ 0.5

During the full year of 2007, the Company expects to recognize approximately $2 million for amortization of accumulated other comprehensive loss related to its U.S. pension and OPEB plans, of which $0.6 and $1.1 million were recognized in the three and six months ended June 30, 2007, respectively.

French Pension Benefits

The components of net pension costs under French plans for the three and six months ended June 30, 2007 and 2006 were as follows (dollars in millions):

French Pension Benefits	**Three Months Ended**		**Six Months Ended**	
	June 30, 2007	**June 30, 2006**	**June 30, 2007**	**June 30, 2006**
Service cost	$ 0.5	$ 0.4	$ 1.0	$ 0.8
Interest cost	0.5	0.5	0.9	1.0
Expected return on plan assets	(0.4)	(0.3)	(0.7)	(0.6)
Amortization and other	0.1	0.2	0.3	0.4
Net periodic benefit cost	$ 0.7	$ 0.8	$ 1.5	$ 1.6

During the full year of 2007, the Company expects to recognize approximately $1 million for amortization of accumulated other comprehensive loss related to its French pension plans, of which $0.1 million and $0.3 million were recognized in the three and six months ended June 30, 2007, respectively.

The Company contributed $4.0 million and $2.0 million to its U.S. and French pension plans through the first six months of 2007 and 2006, respectively, and currently expects to make total pension contributions for the full year of 2007 of approximately $7 to $12 million. The Company also made payments of $1.1 million and $1.2 million in the six months ended June 30, 2007 and 2006, respectively, related to its U.S. OPEB benefits and expects to make payments of approximately $2 million during the full year of 2007.

NOTE 7. PRIOR PERIOD RESTATEMENT

As reported in its Form 10-Q for the quarter ended March 31, 2007, the Company restated its prior period consolidated financial statements to correct an accounting error, which originated in 2003, by recognizing the impact of a French income tax assessment on statutory profit sharing liabilities owed to certain French employees. Under applicable French social law, statutory profit sharing should be recalculated whenever taxable income is adjusted due to a tax audit assessment. In this instance, an audit assessment finalized in 2003 increased prior period statutory taxable earnings, thereby increasing the amount due under the statutory profit sharing regime. However, the Company had not previously recorded the increased profit sharing liability resulting from the French income tax assessment in its 2003 consolidated financial statements.

The increased amount of profit sharing liability was $1.5 million pretax. The after-tax effect of this error on net income in 2003 was $1.0 million. The Company determined that this error did not materially misstate its previously issued financial statements and, in accordance with the provisions of SEC Staff Accounting Bulletin No. 108, the Company restated the accompanying prior period financial statements from amounts previously reported. In years subsequent to 2003, the adjustment was reflected as a reduction of retained earnings of $1.0 million, an increase in other current assets for the deferred income tax effect of $0.5 million and an increase in accrued expenses of $1.5 million.

The effects of the restatement on the consolidated balance sheet as of December 31, 2006 and on the consolidated statements of changes in stockholders equity as of June 30, 2006 and December 31, 2005 were as follows (dollars in millions):

December 31, 2006	**As Previously Reported**	**Error Correction**	**As Restated**
Other current assets	$ 13.8	$ 0.5	$ 14.3
Total Current Assets	235.6	0.5	236.1
Total Assets	696.6	0.5	697.1
Accrued expenses	$ 80.9	$ 1.5	$ 82.4
Total Current Liabilities	166.5	1.5	168.0
Total Liabilities (1)	377.0	1.5	378.5
Retained earnings	$ 271.6	$ (1.0)	$ 270.6
Total Stockholders Equity	304.0	(1.0)	303.0
Total Liabilities and Stockholders Equity	$ 696.6	$ 0.5	$ 697.1
June 30, 2006			
Retained earnings	$ 282.4	$ (1.0)	$ 281.4
Total Stockholders Equity	312.3	(1.0)	311.3
December 31, 2005			
Retained earnings	$ 281.8	$ (1.0)	$ 280.8
Total Stockholders Equity	292.9	(1.0)	291.9

(1) Minority interest of $15.6 million was reclassified from total liabilities at December 31, 2006. The effects of the reclassification on the consolidated balance sheet as of December 31, 2006 were to reduce total liabilities by $15.6 million, and on a separate line report minority interest of $15.6 million.

NOTE 8. SEGMENT INFORMATION

The Company operates and manages 3 reportable segments: United States, or U.S., France and Brazil. These segments are based on the geographical location of the Company s manufacturing operations. These business segments manufacture and sell Cigarette Papers used to wrap various parts of a cigarette and reconstituted tobacco products, as well as certain non-tobacco industry products. While the products are similar in each segment, they vary based on customer requirements and the manufacturing capabilities of each of the operations. Sales by a segment into markets primarily served by a different segment occur where specific product needs cannot be cost-effectively met by the manufacturing operations domiciled in that segment.

The accounting policies of these segments are the same as those described in Note 2, Summary of Significant Accounting Policies, in the Notes to the Consolidated Financial Statements in the Company s Annual Report on Form 10-K for the year ended December 31, 2006. The Company primarily evaluates segment performance and allocates resources based on operating profit and cash flow.

For purposes of the segment disclosure in the following tables, the term United States includes operations in the United States and Canada. The Canadian operations only produce flax fiber used as raw material in the U.S. operations. The term France includes operations in France, the Philippines and Indonesia because the results of the Philippine and Indonesian operations are not material for segment reporting purposes and their sales are integrated with sales of the Company s French operations in southeast Asia. Sales of products between segments are made at market prices and elimination of these sales is referred to in the following tables as intersegment sales. Expense amounts not associated with segments are referred to as unallocated expenses.

Net Sales

(dollars in millions)

	Three Months Ended June 30, 2007		June 30, 2006		Six Months Ended June 30, 2007		June 30, 2006	
France	$ 102.7	59.8 %	$ 97.3	60.0 %	$ 203.0	59.3 %	$ 190.0	58.0 %
United States	56.2	32.7	55.8	34.4	113.1	33.1	118.2	36.1
Brazil	17.1	9.9	14.7	9.1	34.5	10.1	31.0	9.5
Subtotal	176.0	102.4	167.8	103.5	350.6	102.5	339.2	103.6
Intersegment sales by								
France	(1.3)	(0.7)	(3.7)	(2.3)	(2.3)	0.7	(7.1)	(2.2)
United States	(0.7)	(0.4)	(0.2)	(0.1)	(1.5)	0.4	(0.4)	(0.1)
Brazil	(2.2)	(1.3)	(1.8)	(1.1)	(4.7)	1.4	(4.2)	(1.3)
Subtotal	(4.2)	(2.4)	(5.7)	(3.5)	(8.5)	(2.5)	(11.7)	(3.6)
Consolidated	$ 171.8	100.0 %	$ 162.1	100.0 %	$ 342.1	100.0 %	$ 327.5	100.0 %

Operating Profit

(dollars in millions)

	Three Months Ended June 30, 2007		June 30, 2006		Six Months Ended June 30, 2007		June 30, 2006	
France	$ 6.0	100.0 %	$ 5.5	130.9 %	$ 13.2	87.4 %	$ 13.9	105.3 %
United States	3.4	56.7	0.7	16.7				