GRAPHIC PACKAGING HOLDING CO
Form 10-Q
October 25, 2012
Table of Contents

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2012
or
o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from to

COMMISSION FILE NUMBER: 001-33988

Graphic Packaging Holding Company

(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	26-0405422 (I.R.S. employer identification no.)
814 Livingston Court Marietta, Georgia (Address of principal executive offices)	30067 (Zip Code)

(770) 644-3000
(Registrant's telephone number, including area code)

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

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 R No o

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 R Accelerated filer o Non-accelerated filer o Smaller reporting company o
(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 o No R

As of October 19, 2012, there were 393,706,921 shares of the registrant’s Common Stock, par value $0.01 per share, outstanding.

Table of Contents

Information Concerning Forward-Looking Statements

Certain statements regarding the expectations of Graphic Packaging Holding Company (“GPHC” and, together with its subsidiaries, the “Company”), including, but not limited to, statements regarding cost savings from its continuous improvement programs, capital investment, depreciation and amortization, interest expense, net debt reduction, the availability of net operating losses to offset future taxable income, pension plan contributions and postretirement health care benefit payments, in this report constitute “forward-looking statements” as defined in the Private Securities Litigation Reform Act of 1995. Such statements are based on currently available operating, financial and competitive information and are subject to various risks and uncertainties that could cause actual results to differ materially from the Company’s historical experience and its present expectations. These risks and uncertainties include, but are not limited to, inflation of and volatility in raw material and energy costs, continuing pressure for lower cost products, the Company’s ability to implement its business strategies, including productivity initiatives and cost reduction plans, the Company’s debt level, currency movements and other risks of conducting business internationally, and the impact of regulatory and litigation matters, including those that could impact the Company’s ability to utilize its net operating losses to offset taxable income and those that impact the Company's ability to protect and use its intellectual property. Undue reliance should not be placed on such forward-looking statements, as such statements speak only as of the date on which they are made and the Company undertakes no obligation to update such statements. Additional information regarding these and other risks is contained in Part I, “Item 1A., Risk Factors” of the Company’s 2011 Annual Report on Form 10-K, as amended (the "Form 10-K") and in other filings with the Securities and Exchange Commission.

TABLE OF CONTENTS

Table of Contents

PART I — FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

GRAPHIC PACKAGING HOLDING COMPANY
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
In millions, except per share amounts	2012	2011	2012	2011
Net Sales	$1,104.7	$1,073.3	$3,283.8	$3,154.6
Cost of Sales	915.8	919.3	2,728.9	2,677.0
Selling, General and Administrative	95.1	75.8	286.7	255.2
Other Income, Net	(1.0)	(0.4)	(3.0)	(1.6)
Goodwill Impairment, Restructuring and Other Special Charges	3.4	96.3	12.1	96.8
Income (Loss) from Operations	91.4	(17.7)	259.1	127.2
Interest Expense, Net	(26.1)	(34.8)	(85.6)	(110.7)
Loss on Modification or Extinguishment of Debt	—	(1.3)	(8.9)	(2.1)
Income (Loss) before Income Taxes and Equity Income of Unconsolidated Entities	65.3	(53.8)	164.6	14.4
Income Tax (Expense) Benefit	(27.0)	5.6	(68.6)	(4.7)
Income (Loss) before Equity Income of Unconsolidated Entities	38.3	(48.2)	96.0	9.7
Equity Income of Unconsolidated Entities	0.6	0.7	1.6	1.6
Net Income (Loss)	38.9	(47.5)	97.6	11.3
Net Loss Attributable to Noncontrolling Interests	1.2	—	2.1	—
Net Income (Loss) Attributable to Graphic Packaging Holding Company	$40.1	$(47.5)	$99.7	$11.3
Net Income (Loss) Per Share Attributable to Graphic Packaging Holding Company— Basic	$0.10	$(0.12)	$0.25	$0.03
Net Income (Loss) Per Share Attributable to Graphic Packaging Holding Company— Diluted	$0.10	$(0.12)	$0.25	$0.03

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

Table of Contents

GRAPHIC PACKAGING HOLDING COMPANY
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
In millions	2012	2011	2012	2011
Net Income (Loss)	$38.9	$(47.5)	$97.6	$11.3
Other Comprehensive (Loss) Income, Net of Tax:				
Derivative Instruments	(1.8)	4.1	(0.1)	14.6
Currency Translation Adjustment	3.9	(12.3)	2.5	(3.4)
Pension Benefit Plans	4.9	(7.7)	13.6	6.1
Postretirement Benefit Plans	(0.2)	—	(0.6)	(0.5)
Postemployment Benefit Plans	—	—	—	0.1
Total Other Comprehensive Income (Loss), Net of Tax	6.8	(15.9)	15.4	16.9
Total Comprehensive Income (Loss)	45.7	(63.4)	113.0	28.2
Comprehensive Loss Attributable to Noncontrolling Interests	1.2	—	2.0	—
Comprehensive Income (Loss) Attributable to Graphic Packaging Holding Company	$46.9	$(63.4)	$115.0	$28.2

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

Table of Contents

GRAPHIC PACKAGING HOLDING COMPANY
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)

In millions, except share and per share amounts	September 30, 2012	December 31, 2011
ASSETS		
Current Assets:		
Cash and Cash Equivalents	$ 36.5	$ 271.8
Receivables, Net	462.2	401.9
Inventories, Net	503.5	474.2
Deferred Income Tax Assets	63.5	125.0
Other Current Assets	21.0	35.2
Total Current Assets	1,086.7	1,308.1
Property, Plant and Equipment, Net	1,609.7	1,631.7
Goodwill	1,120.7	1,135.7
Intangible Assets, Net	507.6	535.9
Other Assets	46.6	38.3
Total Assets	$ 4,371.3	$ 4,649.7
LIABILITIES		
Current Liabilities:		
Short-Term Debt and Current Portion of Long-Term Debt	$ 64.4	$ 30.1
Accounts Payable	401.0	411.4
Interest Payable	24.9	23.0
Other Accrued Liabilities	197.9	181.0
Total Current Liabilities	688.2	645.5
Long-Term Debt	1,912.8	2,335.7
Deferred Income Tax Liabilities	69.0	63.0
Other Noncurrent Liabilities	401.1	424.0
Redeemable Noncontrolling Interests	13.7	14.8
SHAREHOLDERS' EQUITY		
Preferred Stock, par value $.01 per share; 100,000,000 shares authorized; no shares issued or outstanding	—	—
Common Stock, par value $.01 per share; 1,000,000,000 shares authorized; 393,706,302 and 389,474,786 shares issued and outstanding at September 30, 2012 and December 31, 2011, respectively	3.9	3.9
Capital in Excess of Par Value	2,183.0	2,177.5
Accumulated Deficit	(631.7)	(731.4)

Accumulated Other Comprehensive Loss	(266.8)	(282.1)
Total Graphic Packaging Holding Company Shareholders’ Equity	1,288.4	1,167.9
Noncontrolling Interests	(1.9)	(1.2)
Total Equity	1,286.5	1,166.7
Total Liabilities and Equity	$ 4,371.3	$ 4,649.7

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

Table of Contents

GRAPHIC PACKAGING HOLDING COMPANY
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

In millions	Nine Months Ended September 30, 2012	2011
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net Income	$97.6	$11.3
Non-cash Items Included in Net Income:		
Depreciation and Amortization	202.0	209.2
Goodwill Impairment Charge	—	96.3
Deferred Income Taxes	60.1	(0.7)
Amount of Postretirement Expense Less Than Funding	(11.7)	(30.7)
Other, Net	36.7	24.9
Changes in Operating Assets and Liabilities	(96.4)	(111.4)
Net Cash Provided by Operating Activities	288.3	198.9
CASH FLOWS FROM INVESTING ACTIVITIES:		
Capital Spending	(128.4)	(108.4)
Acquisition of Business	—	(51.9)
Proceeds from Sale of Assets	17.2	—
Other, Net	(3.0)	(2.8)
Net Cash Used in Investing Activities	(114.2)	(163.1)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net Proceeds from Issuance of Common Stock	—	237.7
Repurchase of Common Stock	—	(32.9)
Proceeds from Issuance or Modification of Debt	1,000.0	—
Payments on Debt	(1,690.9)	(223.3)
Borrowings under Revolving Credit Facilities	1,028.6	75.2
Payments under Revolving Credit Facilities	(729.2)	(73.3)
Redemption and Debt Issuance Costs	(22.3)	—
Repurchase of Common Stock related to Share-Based Payments	(10.6)	—
Other, Net	13.7	(0.2)
Net Cash Used in Financing Activities	(410.7)	(16.8)
Effect of Exchange Rate Changes on Cash	1.3	(0.6)
Net (Decrease) Increase in Cash and Cash Equivalents	(235.3)	18.4
Cash and Cash Equivalents at Beginning of Period	271.8	138.7
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$36.5	$157.1

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

Table of Contents
GRAPHIC PACKAGING HOLDING COMPANY
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

NOTE 1 — GENERAL INFORMATION

Nature of Business and Basis of Presentation

Graphic Packaging Holding Company ("GPHC" and, together with its subsidiaries, the "Company") is a leading provider of packaging solutions for a wide variety of products to food, beverage and other consumer products companies. The Company is the largest U.S. producer of folding cartons and holds a leading market position in coated unbleached kraft paperboard, coated-recycled boxboard and flexible packaging. The Company's customers include some of the most widely recognized companies in the world. The Company strives to provide its customers with packaging solutions designed to deliver marketing and performance benefits at a competitive cost by capitalizing on its low-cost paperboard mills and converting plants, its proprietary carton and packaging designs, and its commitment to customer service.

GPHC and Graphic Packaging Corporation ("GPC") conduct no significant business and have no independent assets or operations other than GPHC's ownership of all of GPC's outstanding common stock, and GPC's ownership of all of the outstanding common stock of Graphic Packaging International, Inc. ("GPII").

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

In the Company's opinion, the accompanying Condensed Consolidated Financial Statements contain all normal recurring adjustments necessary to present fairly the financial position, results of operations and cash flows for the interim periods. The Company's year end Condensed Consolidated Balance Sheet data was derived from audited financial statements. The accompanying unaudited Condensed Consolidated Financial Statements have been prepared in accordance with instructions to Form 10-Q and Rule 10-01 of Regulation S-X and do not include all the information required by accounting principles generally accepted in the United States of America ("U.S. GAAP") for complete financial statements. Therefore, these Condensed Consolidated Financial Statements should be read in conjunction with GPHC's Form 10-K for the year ended December 31, 2011. In addition, the preparation of the Condensed Consolidated Financial Statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the Condensed Consolidated Financial Statements and the reported amounts of revenues and expenses during the reporting period. Actual amounts could differ from those estimates and changes in these statements are recorded as known. Certain reclassifications have been made to prior year amounts in order to conform to current year presentation.

For a summary of the Company's significant accounting policies, please refer to GPHC's Form 10-K for the year ended December 31, 2011.

Adoption of New Accounting Standards

Effective January 1, 2012, the Company adopted revised guidance as required by the Intangibles – Goodwill and Other topic of the Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("the FASB

Codification”) which allows an entity to first assess qualitative factors to determine whether it is necessary to perform the two-step quantitative impairment test. The adoption did not have a material impact on the Company’s financial position, results of operations or cash flows.

Effective January 1, 2012, the Company adopted revised guidance as required by the Fair Value Measurement topic of the FASB Codification. This amendment represents the converged guidance of the FASB and the International Accounting Standards Board on fair value measurement, resulting in common requirements for measuring fair value and for disclosing information about fair value measurements. The adoption did not have a material impact on the Company’s financial position, results of operations or cash flows.

Goodwill Impairment, Restructuring and Other Special Charges

The following table summarizes the transactions recorded in Goodwill Impairment, Restructuring and Other Special Charges in the Consolidated Statements of Operations:

	Three Months Ended September 30,		Nine Months Ended September 30,	
In millions	2012	2011	2012	2011
Goodwill Impairment	$—	$96.3	$—	$96.3
Asset Impairment and Shutdown Charges	0.1	—	2.9	—
Charges Associated with Business Combinations	3.3	—	9.2	0.5
Total	$3.4	$96.3	$12.1	$96.8

Table of Contents

NOTE 2 — INVENTORIES, NET

Inventories, Net by major class:

In millions	September 30, 2012	December 31, 2011
Finished Goods	$ 245.9	$ 243.5
Work in Progress	50.9	41.1
Raw Materials	148.5	135.8
Supplies	58.2	53.8
Total	$ 503.5	$ 474.2

NOTE 3 — DEBT

On March 16, 2012, the Company entered into a $2.0 billion amended and restated credit agreement with a syndicate of lenders consisting primarily of commercial banks (the “Credit Agreement”). The Credit Agreement provides for a $1.0 billion revolving credit facility and a $1.0 billion amortizing term loan facility, both due on March 16, 2017. The revolving credit facility and the term loan facility bear interest at an initial rate equal to the London Interbank Offered Rate (LIBOR) plus 225 basis points. The interest rate margin over LIBOR will vary between 175 basis points and 275 basis points depending upon the Company's current consolidated total leverage ratio. Approximately $1.53 billion was drawn at closing which, when combined with cash on hand, was used to repay the approximate $1.68 billion of outstanding term loans due in May 2014. This transaction was treated primarily as an extinguishment of debt, and a charge of $8.9 million was recorded as Loss on Modification or Extinguishment of Debt in the Company's Condensed Consolidated Statements of Operations.

For more information regarding the Company’s debt, see “Note 5 — Debt” of the Notes to Consolidated Financial Statements of the Company’s 2011 Form 10-K.

Long-Term Debt is composed of the following:

In millions	September 30, 2012	December 31, 2011
Senior Notes with interest payable semi-annually at 7.875%, payable in 2018 ($250.0 million face amount)	$ 246.7	$ 246.4
Senior Notes with interest payable semi-annually at 9.5%, payable in 2017 ($425.0 million face amount)	423.2	423.2
Senior Secured Term Loan Facility with interest payable at various dates at floating rates payable through 2014	—	769.0
Senior Secured Term Loan Facility with interest payable at various dates at floating rates payable through 2014	—	908.7
Senior Secured Term Loan Facility with interest payable at various dates at floating rates (2.23% at September 30, 2012) payable through 2017	987.5	—
Senior Secured Revolving Facility with interest payable at floating rates (2.23% at September 30, 2012) payable in 2017	296.0	—

Capital Lease Obligations	5.8	7.3
Other	18.0	11.2
	1,977.2	2,365.8
Less: current portion	64.4	30.1
Total	$1,912.8	$2,335.7

Long-Term Debt maturities (excluding capital leases) are as follows:

In millions	
Remainder of 2012	$18.3
2013	61.1
2014	63.3
2015	87.8
2016	100.0
2017	1,394.2
After 2017	246.7
Total	$1,971.4

At September 30, 2012, the Company and its U.S. and international subsidiaries had the following commitments, amounts outstanding and amounts available under revolving credit facilities:

In millions	Total Commitments	Total Outstanding	Total Available (a)
Revolving Credit Facility	$ 1,000.0	$296.0	$670.7
International Facilities	17.1	12.4	4.7
Total	$ 1,017.1	$308.4	$675.4

Note:

(a) In accordance with its debt agreements, the Company's availability under its Revolving Credit Facility has been reduced by the amount of standby letters of credit issued of $33.3 million as of September 30, 2012. These letters of credit are used primarily as security against its self-insurance obligations and workers' compensation obligations. These letters of credit expire at various dates through 2013 unless extended.

The Credit Agreement and the indentures governing the 9.5% Senior Notes due 2017 and the 7.875% Senior Notes due 2018 (the "Indentures") limit the Company's ability to incur additional indebtedness. Additional covenants contained in the Credit Agreement and the Indentures, among other things, restrict the ability of the Company to dispose of assets, incur guarantee obligations, prepay other indebtedness, make dividend and other restricted payments, create liens, make equity or debt investments, make acquisitions, modify terms of the Indentures, engage in mergers or consolidations, change the business conducted by the Company and its subsidiaries, and engage in certain transactions with affiliates. Such restrictions, together with the highly leveraged nature of the Company, could limit the Company's ability to respond to changing market conditions, fund its capital spending program, provide for unexpected capital investments or take advantage of business opportunities.

Under the terms of the Credit Agreement, the Company must comply with a maximum consolidated total leverage ratio and a minimum consolidated interest coverage ratio. The Company's obligations under the Credit Agreement are secured by substantially all of the Company's domestic assets.

As of September 30, 2012, the Company was in compliance with the covenants in the Credit Agreement and the Indentures.

NOTE 4 — STOCK INCENTIVE PLANS

The Company has four equity compensation plans, but since 2004 the Company's only plan pursuant to which new grants are made is the Graphic Packaging Holding Company Amended and Restated 2004 Stock and Incentive Compensation plan (the "2004 Plan"). Stock options and other awards granted under all of the Company's plans generally vest and expire in accordance with terms established at the time of grant. Shares issued pursuant to awards under the plans are from the Company's authorized but unissued shares. Compensation costs are recognized on a straight-line basis over the requisite service period of the award.

Stock Awards, Restricted Stock and Restricted Stock Units

The Company's 2004 Plan permits the grant of stock awards, restricted stock and restricted stock units ("RSUs"). All RSUs vest and become payable in one to five years from date of grant. RSUs granted to employees generally contain performance conditions based on various financial targets and service requirements that must be met for the shares to vest. Upon vesting, RSUs are payable in cash and shares of common stock, based on the proportion set forth in the grant agreements. Stock awards granted to non-employee directors are unrestricted on the grant date.

Table of Contents

Data concerning RSUs and stock awards granted in the first nine months of 2012 is as follows:

Shares in thousands	Shares	Weighted Average Grant Date Fair Value Per Share
RSUs — Employees	3,742	$5.43
Stock Awards — Board of Directors	207	$5.21

During the nine months ended September 30, 2012 and 2011, $21.2 million and $10.0 million, respectively, were charged to compensation expense for stock incentive plans.

During the nine months ended September 30, 2012, 3.7 million shares were issued. The shares issued were primarily related to RSUs granted during 2009.

During the nine months ended September 30, 2012, 0.3 million shares were issued through the exercise of stock options at an average exercise price of $1.56 per share.

NOTE 5 — PENSIONS AND OTHER POSTRETIREMENT BENEFITS

The Company maintains both defined benefit pension plans and postretirement health care plans that provide medical and life insurance coverage to eligible salaried and hourly retired employees in North America and their dependents. The Company maintains international defined benefit pension plans which are either noncontributory or contributory and are funded in accordance with applicable local laws. Pension or termination benefits are based primarily on years of service and the employees' compensation.

Currently, the North American defined benefit plans are closed to newly-hired salaried and non-union hourly employees. Effective July 1, 2011, the North American defined benefit plans were frozen for most salaried and non-union hourly employees and replaced with a defined contribution plan. The U.K. and Canada defined benefit plans were frozen effective March 31, 2001 and December 31, 2009, respectively, and replaced with defined contribution plans.

Pension and Postretirement Expense

The pension and postretirement expenses related to the Company's plans consisted of the following:

	Pension Benefits				Postretirement Health Care Benefits			
	Three Months Ended September 30,		Nine Months Ended September 30,		Three Months Ended September 30,		Nine Months Ended September 30,	
In millions	2012	2011	2012	2011	2012	2011	2012	2011
Components of Net Periodic Cost:								
Service Cost	$5.1	$4.9	$14.1	$14.5	$0.3	$0.4	$1.0	$1.0
Interest Cost	13.2	13.1	38.3	39.2	0.6	0.7	1.8	2.2
Administrative Expenses	—	—	0.1	0.1	—	—	—	—
Expected Return on Plan Assets	(14.9)	(14.6)	(43.5)	(43.8)	—	—	—	—

Curtailment Loss (Gain)	—	0.2	(0.2)	(0.6)	—	—	—	—
Amortization:								
Prior Service Cost (Credit)	0.3	0.1	0.5	0.3	—	—	(0.1)	(0.1)
Actuarial Loss (Gain)	7.5	3.5	22.5	10.1	(0.3)	(0.2)	(0.9)	(0.6)
Net Periodic Cost	$11.2	$7.2	$31.8	$19.8	$0.6	$0.9	$1.8	$2.5

Employer Contributions

The Company made contributions of $43.8 million and $51.6 million to its pension plans during the first nine months of 2012 and 2011, respectively. The Company expects to make contributions of $45 to $60 million for the full year 2012. During 2011, the Company made $64.5 million of contributions to its pension plans.

The Company made postretirement health care benefit payments of $1.5 million and $1.4 million during the first nine months of 2012 and 2011, respectively. The Company estimates its postretirement health care benefit payments for the full year 2012 to be approximately $3 million. During 2011, the Company made postretirement health care benefit payments of $2.6 million.

NOTE 6 — FINANCIAL INSTRUMENTS AND FAIR VALUE MEASUREMENT

The Company enters into derivative instruments for risk management purposes only, including derivatives designated as hedging instruments under the Derivatives and Hedging topic of the FASB Codification and those not designated as hedging instruments under this guidance. The Company uses interest rate swaps, natural gas swap contracts, and forward exchange contracts. These derivative instruments are designated as cash flow hedges and, to the extent they are effective in offsetting the variability of the hedged cash flows, changes in the derivatives' fair value are not included in current earnings but are included in Accumulated Other Comprehensive Income. These changes in fair value will subsequently be reclassified to earnings.

Interest Rate Risk

The Company uses interest rate swaps to manage interest rate risks on future interest payments caused by interest rate changes on its variable rate term loan facility. The differential to be paid or received under these agreements is recognized as an adjustment to Interest Expense related to debt. At September 30, 2012 and December 31, 2011, the Company had interest rate swap agreements with a notional amount of $460 million and $920 million, respectively. The outstanding swap agreements, under which the Company will pay fixed rates of 0.80% to 0.82% and receive one-month LIBOR rates, expire in April 2016.

Changes in fair value will subsequently be reclassified into earnings as a component of Interest Expense, Net as interest is incurred on amounts outstanding under the term loan facility. Ineffectiveness measured in the hedging relationship is recorded in earnings in the period it occurs.

During the first nine months of 2012 and 2011, there were minimal amounts of ineffectiveness related to changes in the fair value of interest rate swap agreements. Additionally, there were no amounts excluded from the measure of effectiveness.

Commodity Risk

To manage risks associated with future variability in cash flows and price risk attributable to certain commodity purchases, the Company enters into natural gas swap contracts to hedge prices for a designated percentage of its expected natural gas usage. The Company has entered into natural gas swap contracts to hedge pricing for approximately 50% of its expected natural gas usage for the remainder of 2012, with a weighted average contractual rate of $3.07 per one million British Thermal Units ("MMBTUs") and 25% of its expected natural gas usage for the first quarter of 2013, with a weighted average contractual rate of $3.43 per MMBTU. Such contracts are designated as cash flow hedges. The contracts are carried at fair value with changes in fair value recognized in Accumulated Other Comprehensive Loss, and the resulting gain or loss is reclassified into Cost of Sales concurrently with the recognition of the commodity consumed. The ineffective portion of the swap contracts' change in fair value would be recognized immediately in earnings.

During the first nine months of 2012 and 2011, there were minimal amounts of ineffectiveness related to changes in the fair value of natural gas swap contracts. Additionally, there were no amounts excluded from the measure of effectiveness.

Foreign Currency Risk

The Company enters into forward exchange contracts to manage risks associated with future variability in cash flows resulting from anticipated foreign currency transactions that may be adversely affected by changes in exchange rates. Such contracts are designated as cash flow hedges. The contracts are carried at fair value with changes in fair value recognized in Accumulated Other Comprehensive Loss, and gains/losses related to these contracts are recognized in Other Income, Net when the anticipated transaction affects income. At September 30, 2012, multiple forward exchange contracts existed that expire on various dates through 2012. Those purchased forward exchange contracts outstanding at September 30, 2012 and December 31, 2011, when aggregated and measured in U.S. dollars at contractual rates at September 30, 2012 and December 31, 2011 had notional amounts totaling $17.6 million and $79.8 million, respectively.

No amounts were reclassified to earnings during the first nine months of 2012 or during 2011 in connection with forecasted transactions that were no longer considered probable of occurring, and there was no amount of ineffectiveness related to changes in the fair value of foreign currency forward contracts. Additionally, there were no amounts excluded from the measure of effectiveness.

Derivatives not Designated as Hedges

The Company enters into forward exchange contracts to effectively hedge substantially all of its accounts receivable resulting from sales transactions denominated in foreign currencies in order to manage risks associated with foreign currency transactions adversely affected by changes in exchange rates. At September 30, 2012 and December 31, 2011, multiple foreign currency forward exchange contracts existed, with maturities ranging up to three months. Those foreign currency exchange contracts outstanding at September 30, 2012 and December 31, 2011, when aggregated and measured in U.S. dollars at exchange rates at September 30, 2012 and December 31, 2011, had net notional amounts totaling $20.3 million and $19.5 million, respectively. Unrealized gains and losses resulting from these contracts are recognized in Other Income, Net and approximately offset corresponding recognized but unrealized gains and losses on these accounts receivable.

Fair Value of Financial Instruments

The Company's derivative instruments are carried at fair value. The Company has determined that the inputs to the valuation of these derivative instruments are level 2 in the fair value hierarchy. Level 2 inputs are defined as quoted prices for similar assets and liabilities in active markets or inputs that are observable for the asset or liability, either directly or indirectly through market corroboration, for substantially the full term of the financial instrument. The Company uses valuation techniques based on discounted cash flow analyses, which reflects the terms of the derivatives and uses observable market-based inputs, including forward rates and uses market price quotations obtained from independent derivatives brokers, corroborated with information obtained from independent pricing service providers.

As of September 30, 2012, there has not been any significant impact to the fair value of the Company's derivative liabilities due to its own credit risk. Similarly, there has not been any significant adverse impact to the Company's derivative assets based on evaluation of the Company's counterparties' credit risks.

The fair value of the Company's derivative instruments is as follows:

	Derivative Assets			Derivative Liabilities		
In millions	Balance Sheet Location	September 30, 2012	December 31, 2011	Balance Sheet Location	September 30, 2012	December 31, 2011
Derivative Contracts Designated as Hedging Instruments						
Commodity Contracts	Other Current Assets	$ 0.6	$ —	Other Accrued Liabilities	$ —	$ 1.3
Foreign Currency Contracts	Other Current Assets	0.4	1.3	Other Accrued Liabilities	0.1	0.3
Interest Rate Swap Agreements	Other Current Assets	—	—	Other Accrued Liabilities, Other Noncurrent Liabilities and Interest Payable	6.6	8.3
Derivative Contracts Not Designated as Hedging Instruments						
Foreign Currency Contracts	Other Current Assets	—	0.5	Other Accrued Liabilities	0.1	—
Total Derivative Contracts		$ 1.0	$ 1.8		$ 6.8	$ 9.9

The fair values of the Company's other financial assets and liabilities at September 30, 2012 and December 31, 2011 approximately equal the carrying values reported on the Consolidated Balance Sheets except for Long-Term Debt. The fair value of the Company's Long-Term Debt (excluding capital leases) was $2,047.4 million and $2,411.1 million as compared to the carrying amounts of $1,971.4 million and $2,358.5 million as of September 30, 2012 and December 31, 2011, respectively. The fair value of the Company's Senior Notes is based on quoted market prices (Level 1 inputs) and the remainder of the Company's Long-Term Debt is based on Level 2 inputs. Level 2 valuation techniques for Long-Term Debt are based on quotations obtained from independent pricing service providers.

Effect of Derivative Instruments

The pre-tax effect of derivative instruments in cash flow hedging relationships on the Company's Consolidated Statements of Operations is as follows:

Table of Contents
GRAPHIC PACKAGING HOLDING COMPANY
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

In millions	Amount of (Gain) Loss Recognized in Accumulated Other Comprehensive Loss Three Months Ended September 30, 2012	2011	Location in Statement of Operations (Effective Portion)	Amount of (Gain) Loss Recognized in Statement of Operations (Effective Portion) Three Months Ended September 30, 2012	2011	Location in Statement of Operations (Effective Portion)	Amount Recognized in Statement of Operations (Ineffective Portion) Three Months Ended September 30, 2012	2011
Commodity Contracts	$(0.7)	$2.4	Cost of Sales	$(0.1)	$0.4	Cost of Sales	$—	$—
Foreign Currency Contracts	0.3	0.3	Other (Income) Expense, Net	(0.7)	0.6	Other (Income) Expense, Net	—	—
Interest Rate Swap Agreements	3.3	(0.2)	Interest Expense, Net	0.7	5.6	Interest Expense, Net	—	—
Total	$2.9	$2.5		$(0.1)	$6.6		$—	$—

In millions	Amount of Loss (Gain) Recognized in Accumulated Other Comprehensive Loss Nine Months Ended September 30, 2012	2011	Location in Statement of Operations (Effective Portion)	Amount of Loss (Gain) Recognized in Statement of Operations (Effective Portion) Nine Months Ended September 30, 2012	2011	Location in Statement of Operations (Ineffective Portion)	Amount Recognized in Statement of Operations (Ineffective Portion) Nine Months Ended September 30, 2012	2011
Commodity Contracts	$0.3	$3.9	Cost of Sales	$2.9	$2.5	Cost of Sales	$(0.1)	$—
Foreign Currency Contracts	(0.8)	2.3	Other (Income) Expense, Net	(0.6)	1.1	Other (Income) Expense, Net	—	—
Interest Rate Swap Agreements	7.1	1.5	Interest Expense, Net	4.1	18.7	Interest Expense, Net	—	—
Total	$6.6	$7.7		$6.4	$22.3		$(0.1)	$—

The effect of derivative instruments not designated as hedging instruments on the Company’s Condensed Consolidated Statements of Operations is as follows:

In millions		Three Months Ended September 30, 2012	2011	Nine Months Ended September 30, 2012	2011
Foreign Currency Contracts	Other Expense (Income), Net	$1.0	$(1.6)	$0.5	$(0.2)

Accumulated Derivative Instruments (Loss) Income

The following is a rollforward of pre-tax Accumulated Derivative Instruments (Loss) Income which is included in the Company's Condensed Consolidated Balance Sheets:

In millions	
Balance at December 31, 2011	$(4.7)
Reclassification to earnings	6.4
Current period change in fair value	(6.6)
Balance at September 30, 2012	$(4.9)

At September 30, 2012, the Company expects to reclassify approximately $0.9 million of pre-tax loss in the next twelve months from Accumulated Other Comprehensive Loss to earnings, contemporaneously with and offsetting changes in the related hedged exposure. The actual amount that will be reclassified to future earnings may vary from this amount as a result of changes in market conditions.

NOTE 7 — REDEEMABLE NONCONTROLLING INTERESTS

On December 8, 2011, the Company combined its multi-wall bag and specialty plastics packaging businesses with the kraft paper and multi-wall bag businesses of Delta Natural Kraft, LLC and Mid-America Packaging, LLC (collectively "DNK"), both wholly owned subsidiaries of Capital Five Investments, LLC ("CVI"). Under the terms of the transaction, the Company formed a new limited liability company, Graphic Flexible Packaging, LLC ("GFP") and contributed its ownership interests in multi-wall bag and specialty plastics packaging subsidiaries to it. CVI concurrently contributed its ownership interests in DNK to GFP. Neither party received cash consideration as part of the transaction. After the combination, the Company owns approximately 87% of GFP and consolidates its results of operations. The remaining 13% of GFP is owned by CVI. CVI's noncontrolling interest in GFP is recorded as Redeemable Noncontrolling Interests in the Company's financial statements. GFP is included in the flexible segment. This transaction is herein referred to as the "DNK Transaction". The purchase consideration was preliminarily allocated to the assets and liabilities based on estimated fair values as of the purchase date. In connection with the preliminary purchase price allocation, the Company accrued $6.5 million for certain contracts with below-market pricing. Based on the initial independent third party valuation, there were no amounts allocated to goodwill. The Company is in the process of finalizing this valuation and the allocation will be complete during the fourth quarter of 2012. The purchase consideration preliminary allocation did not have a significant impact on the Condensed Consolidated Statements of Operations for the three or nine month periods ended September 30, 2012. In addition, these adjustments did not have a significant impact on the Condensed Consolidated Balance Sheets as of December 31, 2011 or September 30, 2012. Therefore, the Company has not retrospectively adjusted this information.

CVI has the right, at certain times, to require the Company to acquire their ownership interests in GFP at fair value based on third-party valuations. Since it is probable that the noncontrolling interests will become redeemable in the future, based on the passage of time, the noncontrolling interests subject to the put options are adjusted to their estimated redemption amounts each reporting period with a corresponding adjustment to Capital in Excess of Par Value. The adjustment to the carrying amount will be determined after attribution of comprehensive income of the redeemable noncontrolling interests. The adjustment to the carrying amount will not impact net income or comprehensive income in the Company's Condensed Consolidated Financial Statements and will not impact earnings per share since the shares of the redeemable noncontrolling interests are redeemable at fair value. For accounting purposes, the redemption value at which the redeemable noncontrolling interests is recorded on the Condensed Consolidated Balance Sheets cannot be less than the initial amount plus attribution of comprehensive income of the noncontrolling interest. At September 30, 2012, the book value of the redeemable noncontrolling interests was determined as follows:

In millions	
Balance at December 31, 2011	$ 14.8
Initial noncontrolling interests and adjustments related to acquisition	0.2
Net loss attributable to redeemable noncontrolling interests	(1.4)
Other comprehensive income, net of tax	0.1
Change in fair value of redeemable securities	—
Balance at September 30, 2012	$ 13.7

The calculation of fair value (a Level 3 measurement) of the redeemable noncontrolling interest is determined by using a discounted cash flow analysis based on the Company's forecasts discounted using a weighed average cost of capital and market indicators of terminal year cash flows based upon a multiple of EBITDA.

NOTE 8 — INCOME TAXES

During the three months and nine months ended September 30, 2012, the Company recognized Income Tax Expense of $27.0 million and $68.6 million on Income before Income Taxes and Equity Income of Unconsolidated Entities of $65.3 million and $164.6 million, respectively. The effective tax rate for the nine months ended September 30, 2012 was different than the statutory rate primarily due to the mix and levels between foreign and domestic earnings including losses in jurisdictions with full valuation allowances, as well as the effects of certain discrete tax items. During the three months and nine months ended September 30, 2011, the Company recognized Income Tax Benefit (Expense) of $5.6 million and $(4.7) million on (Loss) Income before Income Taxes and Equity Income of Unconsolidated Entities of $(53.8) million and $14.4 million, respectively. Income Tax Benefit (Expense) for the three months and nine months ended September 30, 2011 primarily relates to the $16.3 million benefit related to the non-cash goodwill impairment charge. This benefit was partially offset by the non-cash expense of $5.5 million and $16.7 million, respectively, associated with the amortization of goodwill for tax purposes. During the fourth quarter of 2011, the Company released its U.S. federal and a substantial portion of its state deferred tax valuation allowance. The Company has approximately $1.0 billion of Net Operating Losses for U.S. federal income tax purposes, which are currently being used and may be used to offset future taxable income.

Table of Contents
GRAPHIC PACKAGING HOLDING COMPANY
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

NOTE 9 — ENVIRONMENTAL AND LEGAL MATTERS

Environmental Matters

The Company is subject to a broad range of foreign, federal, state and local environmental, health and safety laws and regulations, including those governing discharges to air, soil and water, the management, treatment and disposal of hazardous substances, solid waste and hazardous wastes, the investigation and remediation of contamination resulting from historical site operations and releases of hazardous substances, and the health and safety of employees. Compliance initiatives could result in significant costs, which could negatively impact the Company’s consolidated financial position, results of operations or cash flows. Any failure to comply with environmental or health and safety laws and regulations or any permits and authorizations required thereunder could subject the Company to fines, corrective action or other sanctions.

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

The Company has established reserves for those facilities or issues where liability is probable and the costs are reasonably estimable. The Company believes that the amounts accrued for all of its loss contingencies, and the reasonably possible loss beyond the amounts accrued, are not material to the Company’s consolidated financial position, results of operations or cash flows. The Company cannot estimate with certainty other future corrective compliance, investigation or remediation costs. Costs relating to historical usage that the Company considers to be reasonably possible of resulting in liability are not quantifiable at this time. The Company will continue to monitor environmental issues at each of its facilities, as well as regulatory developments, and will revise its accruals, estimates and disclosures relating to past, present and future operations, as additional information is obtained.

Legal Matters

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

NOTE 10 — SEGMENT INFORMATION

The Company reports its results in two reportable segments: paperboard packaging and flexible packaging. These segments are evaluated by the chief operating decision maker based primarily on Income from Operations as adjusted for depreciation and amortization. The Company’s reportable segments are based upon strategic business units that offer different products. As a result of January 2012 changes in the Company's internal reporting structure, the Company's Labels business is now a part of the paperboard packaging segment. The Company's 2011 segment results including certain corporate allocations have been reclassified to be consistent with the current year presentation. The accounting policies of the reportable segments are the same as those described in GPHC's Form 10-K for the year ended December 31, 2011.

The paperboard packaging segment is highly integrated and includes a system of mills and plants that produce a broad range of paperboard grades convertible into folding cartons. Folding cartons are used primarily to protect products, such as food, detergents, paper products, beverages, and health and beauty aids, while providing point of purchase advertising. The paperboard packaging reportable segment includes the design, manufacture and installation of packaging machinery related to the assembly of cartons, the production and sale of corrugated medium and kraft paper from paperboard mills in the U.S, and produces paper and heat transfer labels.

The flexible packaging segment produces kraft paper and converts kraft and specialty paper into multi-wall bags, consumer and specialty retail bags and produces flexible packaging and laminations. The multi-wall bags are designed to ship and protect a wide range of industrial and consumer products including fertilizers, chemicals, concrete, and pet and food products. The flexible packaging and laminations are converted from a wide variety of technologically advanced films for use in the food, pharmaceutical and industrial end-markets. Flexible packaging paper is used in a wide range of consumer applications.

Table of Contents
GRAPHIC PACKAGING HOLDING COMPANY
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

Segment information is as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
In millions	2012	2011	2012	2011
NET SALES:				
Paperboard Packaging	$929.0	$913.4	$2,740.4	$2,684.1
Flexible Packaging	175.7	159.9	543.4	470.5
Total	$1,104.7	$1,073.3	$3,283.8	$3,154.6
INCOME (LOSS) FROM OPERATIONS:				
Paperboard Packaging	$115.3	$96.8	$325.4	$272.4
Flexible Packaging	(9.4)	(97.3)	(18.3)	(97.7)
Corporate	(14.5)	(17.2)	(48.0)	(47.5)
Total	$91.4	$(17.7)	$259.1	$127.2
DEPRECIATION AND AMORTIZATION:				
Paperboard Packaging	$57.8	$61.9	$174.9	$184.4
Flexible Packaging	8.4	7.2	24.9	22.7
Corporate	1.0	0.7	2.2	2.1
Total	$67.2	$69.8	$202.0	$209.2

NOTE 11 — EARNINGS PER SHARE

	Three Months Ended September 30,		Nine Months Ended September 30,	
In millions, except per share data	2012	2011	2012	2011
Net Income (Loss) Attributable to Graphic Packaging Holding Company	$40.1	$(47.5)	$99.7	$11.3
Weighted Average Shares:				
Basic	396.1	390.6	394.8	371.4
Dilutive Effect of Stock Awards	2.1	—	2.7	5.4
Diluted	398.2	390.6	397.5	376.8
Earnings Per Share — Basic	$0.10	$(0.12)	$0.25	$0.03
Earnings Per Share — Diluted	$0.10	$(0.12)	$0.25	$0.03

The following are the potentially dilutive securities excluded from the above calculation because the effect would have been anti-dilutive:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2012	2011	2012	2011
Employee Stock Options	2,346,818	5,206,917	2,346,818	4,633,817
Restricted Stock Units	—	7,817,109	—	—

Total	2,346,818	13,024,026	2,346,818	4,633,817

Table of Contents
GRAPHIC PACKAGING HOLDING COMPANY
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

NOTE 12 — EQUITY

The following is a summary of the changes in total equity for the nine months ended September 30, 2012:

In millions	Graphic Packaging Holding Company Shareholders Equity	Noncontrolling Interests [a]	Total Equity
Balance at December 31, 2011	$1,167.9	$(1.2)	$1,166.7
Net Income (Loss)	99.7	(0.7)	99.0
Other Comprehensive Income, Net of Tax	15.3	—	15.3
Initial Noncontrolling Interests and Adjustments Related to Acquisition	0.7	—	0.7
Compensation Expense Under Share-Based Plans	14.0	—	14.0
Issuance of Common Stock, Net of Stock Received for Minimum Tax Withholdings	(9.2)	—	(9.2)
Balance at September 30, 2012	$1,288.4	$(1.9)	$1,286.5

[a] Excludes amounts related to contingently redeemable noncontrolling interests which are separately classified outside of permanent equity in the mezzanine section of the Condensed Consolidated Balance Sheets.

Table of Contents
GRAPHIC PACKAGING HOLDING COMPANY
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

NOTE 13 — GUARANTOR CONDENSED CONSOLIDATING FINANCIAL STATEMENTS
These consolidating financial statements reflect GPHC and GPC (collectively the "Parent"); GPII, the issuer of the Company's Senior Notes (the "Subsidiary Issuer"); and the Subsidiary Guarantors, which consist of all material 100% owned subsidiaries of GPII other than its foreign subsidiaries; and the nonguarantor subsidiaries are herein referred to as "Nonguarantor Subsidiaries." The Nonguarantor Subsidiaries include all of GPII's foreign subsidiaries and the subsidiaries of GFP. The consolidating financial statements as of and for the period ended September 30, 2011 have been reclassified to include the subsidiaries of GFP contributed by GPII as Nonguarantor Subsidiaries, which were previously included as Subsidiary Guarantors. Separate complete financial statements of the Subsidiary Guarantors are not presented because the guarantors are jointly and severally, fully and unconditionally liable under the guarantees.

	Three Months Ended September 30, 2012					
In millions	Parent	Subsidiary Issuer	Combined Guarantor Subsidiaries	Combined Nonguarantor Subsidiaries	Consolidating Eliminations	Consolidated
Net Sales	$—	$ 886.5	$ 15.3	$ 269.0	$ (66.1)	$ 1,104.7
Cost of Sales	—	720.5	11.6	249.8	(66.1)	915.8
Selling, General and Administrative	—	74.2	1.9	19.0	—	95.1
Other (Income) Expense, Net	—	(1.4)	(0.1)	0.5	—	(1.0)
Goodwill Impairment, Restructuring and Other Special Charges	—	0.2	—	3.2	—	3.4
Income (Loss) from Operations	—	93.0	1.9	(3.5)	—	91.4
Interest Expense, Net	—	(24.2)	—	(1.9)	—	(26.1)
Income (Loss) before Income Taxes and Equity Income of Unconsolidated Entities	—	68.8	1.9	(5.4)	—	65.3
Income Tax Expense	—	(26.5)	(1.2)	0.7	—	(27.0)
Income (Loss) before Equity Income of Unconsolidated Entities	—	42.3	0.7	(4.7)	—	38.3
Equity Income of Unconsolidated Entities	—	—	—	0.6	—	0.6
Equity in Net Earnings of Subsidiaries	38.9	(3.4)	(1.2)	—	(34.3)	—
Net Income (Loss)	38.9	38.9	(0.5)	(4.1)	(34.3)	38.9
Net Loss Attributable to Noncontrolling Interests	1.2	1.2	—	—	(1.2)	1.2
Net Income (Loss) Attributable to Graphic Packaging Holding Company	$40.1	$ 40.1	$ (0.5)	$ (4.1)	$ (35.5)	$ 40.1
Comprehensive Income (Loss) Attributable to Graphic Packaging Holding Company	$46.9	$ 46.9	$ (0.7)	$ 0.1	$ (46.3)	$ 46.9

Table of Contents
GRAPHIC PACKAGING HOLDING COMPANY
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

	Three Months Ended September 30, 2011					
In millions	Parent	Subsidiary Issuer	Combined Guarantor Subsidiaries	Combined Nonguarantor Subsidiaries	Consolidating Eliminations	Consolidated
Net Sales	$—	$ 855.3	$ 15.5	$ 268.7	$ (66.2)	$ 1,073.3
Cost of Sales	—	726.8	11.0	247.7	(66.2)	919.3
Selling, General and Administrative	—	58.5	1.8	15.5	—	75.8
Other Expense (Income), Net	—	0.6	0.6	(1.6)	—	