

Neenah Paper Inc
Form 10-Q
November 05, 2010
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2010

OR

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

For the transition period from to

Commission File Number: 001-32240

NEENAH PAPER, INC.

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of
incorporation or organization)

20-1308307

(I.R.S. Employer
Identification No.)

3460 Preston Ridge Road

Alpharetta, Georgia

(Address of principal executive offices)

30005

(Zip Code)

(678) 566-6500

(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§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, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer

Accelerated filer

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

Smaller reporting company

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

As of October 29, 2010, there were approximately 14,760,000 shares of the Company's common stock outstanding.

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(In millions, except share and per share data)

(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Net sales	\$ 161.5	\$ 150.1	\$ 497.4	\$ 419.4
Cost of products sold	133.7	121.8	405.1	346.4
Gross profit	27.8	28.3	92.3	73.0
Selling, general and administrative expenses	16.6	18.1	51.6	51.0
Restructuring costs (Note 4)		(0.4)		17.6
Other income - net	(0.5)	(0.1)	(1.1)	(0.7)
Operating income	11.7	10.7	41.8	5.1
Interest expense - net	4.8	5.4	15.5	16.4
Income (loss) from continuing operations before income taxes	6.9	5.3	26.3	(11.3)
Provision (benefit) for income taxes	2.2	1.9	8.0	(5.4)
Income (loss) from continuing operations	4.7	3.4	18.3	(5.9)
Income (loss) from discontinued operations, net of income taxes (Note 5)	(0.6)	(0.2)	134.0	(0.2)
Net income (loss)	\$ 4.1	\$ 3.2	\$ 152.3	\$ (6.1)
Earnings (Loss) Per Common Share				
Basic				
Continuing operations	\$ 0.32	\$ 0.23	\$ 1.24	\$ (0.40)
Discontinued operations	(0.04)	(0.01)	9.06	(0.01)
	\$ 0.28	\$ 0.22	\$ 10.30	\$ (0.41)
Diluted				
Continuing operations	\$ 0.30	\$ 0.23	\$ 1.18	\$ (0.40)
Discontinued operations	(0.04)	(0.01)	8.64	(0.01)
	\$ 0.26	\$ 0.22	\$ 9.82	\$ (0.41)
Weighted Average Common Shares Outstanding (in thousands)				
Basic	14,763	14,656	14,727	14,652
Diluted	15,620	14,850	15,448	14,652
Cash Dividends Declared Per Share of Common Stock				
	\$ 0.10	\$ 0.10	\$ 0.30	\$ 0.30

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See Notes to Condensed Consolidated Financial Statements

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NEENAH PAPER, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

(In millions)

(Unaudited)

	September 30, 2010	December 31, 2009
ASSETS		
Current Assets		
Cash and cash equivalents	\$ 38.7	\$ 5.6
Accounts receivable (less allowances of \$2.1 million and \$1.9 million)	81.1	67.7
Inventories	71.3	70.7
Income taxes receivable		0.8
Deferred income taxes	14.7	61.7
Prepaid and other current assets	12.0	13.7
Assets held for sale (Note 6)	6.2	10.0
Total Current Assets	224.0	230.2
Property, Plant and Equipment, at cost	568.2	569.6
Less accumulated depreciation	302.8	285.2
Property, plant and equipment net	265.4	284.4
Deferred Income Taxes	49.4	36.5
Goodwill	42.6	44.9
Intangible Assets net	25.0	27.5
Other Assets	12.0	13.1
TOTAL ASSETS	\$ 618.4	\$ 636.6
LIABILITIES AND STOCKHOLDERS EQUITY		
Current Liabilities		
Debt payable within one year	\$ 14.0	\$ 55.6
Accounts payable	31.7	27.2
Accrued expenses	55.3	48.6
Total Current Liabilities	101.0	131.4
Long-term Debt	232.4	263.6
Deferred Income Taxes	21.5	23.7
Noncurrent Employee Benefits	98.5	105.0
Other Noncurrent Obligations	2.9	3.3
TOTAL LIABILITIES	456.3	527.0
Contingencies and Legal Matters (Note 11)		
TOTAL STOCKHOLDERS EQUITY	162.1	109.6
TOTAL LIABILITIES AND STOCKHOLDERS EQUITY	\$ 618.4	\$ 636.6

See Notes to Condensed Consolidated Financial Statements

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NEENAH PAPER, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In millions)

(Unaudited)

	Nine Months Ended September 30,	
	2010	2009
OPERATING ACTIVITIES		
Net income (loss)	\$ 152.3	\$ (6.1)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and amortization	23.4	25.5
Stock-based compensation	3.7	3.5
Deferred income tax provision (benefit)	33.8	(7.8)
Ripon Mill non-cash charges		6.3
Gain on sale of the Woodlands (Note 5)	(74.1)	
Reclassification of cumulative translation adjustments related to investments in Canada (Note 3 and Note 5)	(87.9)	
Decrease (increase) in working capital	(1.9)	29.8
Pension and other postretirement benefits	(6.1)	4.2
Other	(0.8)	(1.0)
NET CASH PROVIDED BY OPERATING ACTIVITIES	42.4	54.4
INVESTING ACTIVITIES		
Capital expenditures	(10.9)	(6.0)
Increase in investments	(1.4)	
Net proceeds from sale of the Woodlands	78.0	
Proceeds from asset sales	0.1	0.7
Other	1.0	(0.6)
NET CASH PROVIDED BY (USED IN) INVESTING ACTIVITIES	66.8	(5.9)
FINANCING ACTIVITIES		
Proceeds from issuance of long-term debt		5.5
Repayments of long-term debt	(70.5)	(41.9)
Short-term borrowings	9.2	7.0
Repayments of short-term debt	(10.6)	(12.5)
Proceeds from exercise of stock options	0.3	
Cash dividends paid	(4.4)	(4.4)
Other	(0.2)	(0.1)
NET CASH USED IN FINANCING ACTIVITIES	(76.2)	(46.4)
EFFECT OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS	0.1	
NET INCREASE IN CASH AND CASH EQUIVALENTS	33.1	2.1
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	5.6	3.3
CASH AND CASH EQUIVALENTS, END OF PERIOD	\$ 38.7	\$ 5.4
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Cash paid during period for interest, net of interest expense capitalized	\$ 10.7	\$ 10.8
Cash paid (received) during period for income taxes	\$ 0.1	\$ (8.2)
Non-cash investing activities:		
Liability for equipment acquired	\$ 1.4	\$ 0.6

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See Notes to Condensed Consolidated Financial Statements

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NEENAH PAPER, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Tabular amounts in millions, except as noted)

Note 1. Background and Basis of Presentation

Background

Neenah Paper, Inc. (Neenah or the Company), is a Delaware corporation incorporated in April 2004. The Company has two primary operations: its technical products business and its fine paper business.

The technical products business is a leading international producer of transportation and other filter media, durable, saturated and coated substrates for a variety of end uses and nonwoven wall coverings. The fine paper business is a leading producer of premium writing, text, cover and specialty papers used in corporate identity packages, corporate annual reports, invitations, personal stationery and high-end packaging for point of sale advertising.

In March 2010, the Company's wholly owned subsidiary, Neenah Paper Company of Canada (Neenah Canada) sold approximately 475,000 acres of woodland assets in Nova Scotia (the Woodlands) to Northern Timber Nova Scotia Corporation, an affiliate of Northern Pulp Nova Scotia Corporation (collectively, Northern Pulp), for C\$82.5 million (\$78.6 million). The sale resulted in a pre-tax gain, net of fees and other transaction costs, of \$74.1 million. The sale of the Woodlands resulted in the substantially complete liquidation of the Company's investment in Neenah Canada. In accordance with Accounting Standards Codification (ASC) Topic 830, *Foreign Currency Matters* (ASC Topic 830), \$87.9 million of cumulative currency translation adjustments attributable to the Company's Canadian subsidiaries have been reclassified into earnings and recognized as part of the gain on sale of the Woodlands. The transaction did not generate a cash tax liability because the tax basis for the Woodlands was approximately equal to the sale price. See Note 5, Discontinued Operations.

For the nine months ended September 30, 2010, the results of operations, the gain on sale of the Woodlands (\$74.1 million) and the reclassification into earnings of cumulative currency translation adjustments attributable to the Company's Canadian subsidiaries (\$87.9 million) are reported as discontinued operations in the condensed consolidated statements of operations. The results of operations of the Woodlands are reported as discontinued operations for the three and nine months ended September 30, 2009. See Note 5, Discontinued Operations.

Basis of Consolidation and Presentation

These statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (the SEC) and, in accordance with those rules and regulations, do not include all information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America (GAAP). Management believes that the

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disclosures made are adequate for a fair presentation of the Company's results of operations, financial position and cash flows. In the opinion of management, the condensed consolidated financial statements reflect all adjustments, consisting only of normal recurring adjustments, necessary to present fairly the results of operations, financial position and cash flows for the interim periods presented herein. The preparation of condensed consolidated financial statements in conformity with GAAP requires management to make extensive use of estimates and assumptions that affect the reported amounts and disclosures. Actual results may vary from these estimates.

These condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company's most recent Annual Report on Form 10-K. The results of operations for any interim period are not necessarily indicative of the results of operations to be expected for the full year.

The condensed consolidated financial statements of Neenah and its subsidiaries included herein are unaudited, except for the December 31, 2009 condensed consolidated balance sheet, which was derived from audited financial statements. The condensed consolidated financial statements include the financial statements of the Company and its wholly owned and majority owned subsidiaries. All significant intercompany balances and transactions have been eliminated from the condensed consolidated financial statements.

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Prior Period Adjustments

During the preparation of the interim financial statements for the three and nine months ended September 30, 2010, the Company identified a \$2.8 million overstatement of accounts payable that was primarily the result of invalid inventory pricing adjustments beginning in 2006 and certain inventory transactions in 2008. These errors resulted in an overstatement of accounts payable and cost of products sold of \$0.3 million and \$2.5 million for the years ended December 31, 2006 and 2008, respectively. The Company has reflected the correction of the errors on the condensed consolidated balance sheet as of December 31, 2009 with a decrease in accounts payable of \$2.8 million, a decrease of \$0.9 million in noncurrent deferred income tax assets and an increase of \$1.9 million in stockholders' equity. The errors in prior periods will be corrected in future filings when presented. The Company believes the effects of these prior period corrections are not material to any prior period consolidated financial statements.

Earnings (Loss) per Share (EPS)

The Company computes basic earnings (loss) per share (EPS) in accordance with ASC Topic 260, *Earnings Per Share* (ASC Topic 260). In accordance with ASC Topic 260, share-based awards with non-forfeitable dividends are classified as participating securities. In calculating basic earnings per share, this method requires net income to be reduced by the amount of dividends declared in the current period for each participating security and by the contractual amount of dividends or other participation payments that are paid or accumulated for the current period. Undistributed earnings for the period are allocated to participating securities based on the contractual participation rights of the security to share in those current earnings assuming all earnings for the period are distributed. Holders of restricted stock, restricted stock units (RSUs) and target performance unit awards (Performance Units) have contractual participation rights that are equivalent to those of common stockholders. Therefore, the Company allocates undistributed earnings to restricted stock, RSUs, Performance Units and common stockholders based on their respective average ownership percentages for the period.

ASC Topic 260 also requires companies with participating securities to calculate diluted earnings per share using the Two-Class method. The Two-Class method requires the denominator to include the weighted average participating securities along with the additional share equivalents from the assumed conversion of stock options calculated using the Treasury Stock method, subject to the anti-dilution provisions of ASC Topic 260.

Diluted EPS was calculated to give effect to all potentially dilutive common shares using the Treasury Stock method. Outstanding stock options, stock appreciation rights (SARs), RSUs and Performance Units represent the only potentially dilutive security effects on the Company's weighted-average shares. For the three and nine months ended September 30, 2010, approximately 1,705,000 and 1,610,000 potentially dilutive stock-based compensation awards, respectively, were excluded from the computation of dilutive common shares because the exercise price of such awards exceeded the average market price of the Company's common stock for the period the awards were outstanding. For the three and nine months ended September 30, 2009, approximately 1,945,000 and 1,755,000 potentially dilutive stock-based compensation awards, respectively, were excluded from the computation of dilutive common shares because the exercise price of such awards exceeded the average market price of the Company's common stock for the period the awards were outstanding. In addition, as a result of the loss from continuing operations for the nine months ended September 30, 2009, approximately 105,000 incremental shares resulting from the assumed vesting of potentially dilutive securities were excluded from the diluted earnings per share calculation, as the effect would have been anti-dilutive.

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The following table presents the computation of basic and diluted EPS (dollars in millions except per share amounts, shares in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Income (loss) from continuing operations	\$ 4.7	\$ 3.4	\$ 18.3	\$ (5.9)
Less: Distributed and undistributed amounts allocated to participating securities (a)			0.1	
Income (loss) from continuing operations available to common stockholders	4.7	3.4	18.2	(5.9)
Income (loss) from discontinued operations, net of income taxes	(0.6)	(0.2)	134.0	(0.2)
Less: Undistributed amounts allocated to participating securities (a)			0.5	
Net income (loss) available to common stockholders	\$ 4.1	\$ 3.2	\$ 151.7	\$ (6.1)
Weighted-average basic shares outstanding	14,763	14,656	14,727	14,652
Add: Assumed incremental shares under stock compensation plans	857	194	721	
Weighted-average diluted shares	15,620	14,850	15,448	14,652
Earnings (Loss) Per Common Share				
Basic				
Continuing operations	\$ 0.32	\$ 0.23	\$ 1.24	\$ (0.40)
Discontinued operations	(0.04)	(0.01)	9.06	(0.01)
	\$ 0.28	\$ 0.22	\$ 10.30	\$ (0.41)
Diluted				
Continuing operations	\$ 0.30	\$ 0.23	\$ 1.18	\$ (0.40)
Discontinued operations	(0.04)	(0.01)	8.64	(0.01)
	\$ 0.26	\$ 0.22	\$ 9.82	\$ (0.41)

(a) In accordance with ASC Topic 260, for the nine months ended September 30, 2009, undistributed losses have been entirely allocated to common stockholders because the holders of participating securities are not contractually obligated to share in the losses of the Company.

Note 2. Accounting Standard Changes

As of September 30, 2010, no amendments to the ASC had been issued that will have or are reasonably likely to have a material effect on the Company's financial position, results of operations or cash flows.

Note 3. Comprehensive Income (Loss)

Comprehensive income (loss) includes, in addition to net income (loss), gains and losses recorded directly into stockholders' equity on the condensed consolidated balance sheet. These gains and losses are referred to as other comprehensive income items. Accumulated other comprehensive income (loss) consists of foreign currency translation gains and (losses) and adjustments related to pensions and other

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postretirement benefits. The Company does not provide income taxes for foreign currency translation adjustments related to indefinite investments in foreign subsidiaries. The sale of the Woodlands resulted in the substantially complete liquidation of the Company's investment in Neenah Canada. In accordance with ASC Topic 830, for the nine months ended September 30, 2010, \$87.9 million of cumulative currency translation adjustments attributable to the Company's Canadian subsidiaries have been reclassified into earnings and recognized as part of the gain on sale of the Woodlands. There were no tax consequences related to the repatriation of funds from the sale of the Woodlands. As of September 30, 2010 and December 31, 2009, accumulated other comprehensive income (loss) was \$(7.7) million and \$91.5 million, respectively.

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The following table presents the components of comprehensive income (loss):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Net income (loss)	\$ 4.1	\$ 3.2	\$ 152.3	\$ (6.1)
Other comprehensive income (loss):				
Unrealized foreign currency translation gain (loss)	19.7	7.6	(10.2)	8.1
Reclassification of cumulative translation adjustments related to investments in Canada			(87.9)	
Adjustments to pension and other post-employment benefit liabilities, net of income taxes	(0.1)	0.1	(1.1)	1.4
Total other comprehensive income (loss)	19.6	7.7	(99.2)	9.5
Comprehensive income	\$ 23.7	\$ 10.9	\$ 53.1	\$ 3.4

Note 4. Closure of the Ripon Mill

In May 2009, the Company permanently closed its fine paper mill located in Ripon, California (the Ripon Mill). For the nine months ended September 30, 2009, the closure resulted in a pre-tax charge of \$17.6 million. The charge was comprised of approximately \$6.3 million in non-cash charges primarily for losses related to the carrying value of property, plant and equipment, a curtailment loss of \$0.8 million related to postretirement benefit plans in which employees of the Ripon Mill participated and cash payments for contract terminations and severance and other employee costs of approximately \$10.5 million.

As of September 30, 2010, the remaining long-lived assets of the Ripon Mill, primarily composed of land and buildings, are classified as assets held for sale on the condensed consolidated balance sheet. The Company believes that the sale of such assets will be completed within 12 months. Assets held for sale are valued at the lower of cost or fair value less cost to sell. The assets of the Ripon Mill are reported at their aggregate historical cost of \$6.2 million. On October 27, 2010, the Company sold the remaining assets of the Ripon Mill for gross proceeds of approximately \$9 million. See Note 14, Subsequent Event.

The Company accounted for costs associated with the closure of the Ripon Mill in accordance with ASC Topic 420, *Exit or Disposal Cost Obligations*. The Company expects the payments of all costs related to the closure of the Ripon Mill to be substantially complete by December 31, 2010. The following table presents the status of such closure costs as of September 30, 2010:

	Severance benefits	Contract termination and other costs	Total
Amounts accrued during the year ended December 31, 2009	\$ 1.8	\$ 8.7	\$ 10.5
Payments for the year ended December 31, 2009	(1.7)	(4.8)	(6.5)
Accrued exit costs at December 31, 2009	0.1	3.9	4.0
Payments for the nine months ended September 30, 2010		(3.4)	(3.4)
Accrued exit costs at September 30, 2010	\$ 0.1	\$ 0.5	\$ 0.6

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In March 2010, Neenah Canada sold the Woodlands to Northern Pulp for C\$82.5 million (\$78.6 million). The sale resulted in a pre-tax gain, net of fees and other transaction costs, of \$74.1 million. The sale of the Woodlands resulted in the substantially complete liquidation of the Company's investment in Neenah Canada. In accordance with ASC Topic 830, \$87.9 million of cumulative currency translation adjustments attributable to the Company's Canadian subsidiaries have been reclassified into earnings and recognized as part of the gain on sale of the Woodlands. The sale of the Woodlands represented the cessation of the Company's operating activities in Canada; however, the Company will have certain continuing post-employment benefit obligations related to its Canadian operations. The transaction did not generate a cash tax liability because the tax basis for the Woodlands was approximately equal to the sale price.

Net proceeds from the sale were used to repay in full \$40 million of outstanding term loan borrowings (the Term Loan) and repay approximately \$26 million in outstanding revolving loans which reduced the balance of such outstanding loans under the Company's bank credit agreement (the Bank Credit Agreement) to zero. In addition, the Company made approximately \$3.1 million in contract termination payments related to the closure of the Ripon Mill that became due and payable upon the sale of the Woodlands.

In June 2008, Neenah Canada sold the Pictou Mill to Northern Pulp. Pursuant to the terms of the transaction, Northern Pulp assumed all of the assets and liabilities associated with the Pictou Mill, as well as existing customer contracts, supply agreements, labor agreements and pension obligations.

In conjunction with the sale of the Pictou Mill, the Company entered into a stumpage agreement (the Stumpage Agreement) which allowed Northern Pulp to harvest softwood timber annually from the Woodlands. The Stumpage Agreement was terminated in March 2010 in conjunction with the sale of the Woodlands. For the nine months ended September 30, 2010, the Company recognized revenue of approximately \$1.4 million, related to timber sales pursuant to the Stumpage Agreement. For the three and nine months ended September 30, 2009, the Company recognized revenue of approximately \$1.2 million and \$2.5 million, respectively, related to the Stumpage Agreement.

The results of operations of the Woodlands and the gain on sale of the Woodlands are reported as discontinued operations in the condensed consolidated statements of operations for each period presented. The following table summarizes the results of discontinued operations:

	Three Months Ended September 30,		Nine Months Ended September 30,		
	2010	2009	2010	2009	
Net sales (a)	\$	\$	1.2	\$	2.5
Income (loss) from discontinued operations:					
Income (loss) from operations before income taxes	\$	(0.1)			