GLATFELTER P H CO
Form 10-K
March 08, 2013
**Table of Contents**

# UNITED STATES SECURITIES AND EXCHANGE COMMISSION

## WASHINGTON, D.C. 20549

# FORM 10-K

þ **Annual report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
**For the fiscal year ended December 31, 2012**

**or**

¨ **Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
**For the transition period from to**

96 South George Street, Suite 520

York, Pennsylvania 17401

*(Address of principal executive offices)*

(717) 225-4711

*(Registrant s telephone number, including area code)*

| Commission file number | Exact name of registrant as specified in its charter | IRS Employer Identification No. | State or other jurisdiction of incorporation or organization |
|---|---|---|---|
| 1-03560 | P. H. Glatfelter Company | 23-0628360 | Pennsylvania |

Securities registered pursuant to Section 12(b) of the Act:

| Title of Each Class | Name of Each Exchange on which registered |
|---|---|
| Common Stock, par value $.01 per share | New York Stock Exchange |

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

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

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 þ 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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes þ No ¨.

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ¨

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

| | | | |
|---|---|---|---|
| Large accelerated filer ¨ | Accelerated filer þ | Non-accelerated filer ¨<br>(Do not check if a smaller reporting company). | Small 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 þ.

Based on the closing price as of June 30, 2012, the aggregate market value of the Common Stock of the Registrant held by non-affiliates was $692.9 million.

**Common Stock outstanding on February 28, 2013 totaled 42,824,288 shares.**

**DOCUMENTS INCORPORATED BY REFERENCE**

Portions of the following documents are incorporated by reference in this Annual Report on Form 10-K:

Portions of the registrant s Proxy Statement to be dated on or about April 3, 2013 are incorporated by reference into Part III.

**Table of Contents**

**P. H. GLATFELTER COMPANY**

**ANNUAL REPORT ON FORM 10-K**

**For the Year Ended**

**DECEMBER 31, 2012**

**Table of Contents**

Table of Contents

**PART I**

We make regular filings with the Securities and Exchange Commission (SEC), including this Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, and Current Reports on Form 8-K. These filings are available, free of charge, on our website, www.glatfelter.com, and the SEC website at www.sec.gov. We also provide copies of our SEC filings at no charge upon request to Investor Relations at (717) 225-2719, ir@glatfelter.com, or by mail to Investor Relations, 96 South George Street, Suite 520, York, PA, 17401. In this filing, unless the context indicates otherwise, the terms we, us, our, the Company, or Glatfelter refer to P. H. Glatfelter Company and subsidiaries.

***ITEM 1 BUSINESS***

**Overview** Glatfelter began operations in 1864, and we believe we are one of the world s leading manufacturers of specialty papers and fiber-based engineered materials. Headquartered in York, Pennsylvania, we own and operate manufacturing facilities located in Pennsylvania, Ohio, Canada, Germany, the United Kingdom, France, and the Philippines.

**Products** Our three business units manufacture a wide array of specialty papers and fiber-based engineered materials including:

- *Specialty Papers* with revenues from the sale of papers for carbonless and other forms, book publishing, envelopes, and engineered products such as papers for digital imaging, casting, release, transfer, playing card, postal, FDA-compliant food and beverage applications, and other niche specialty applications;

- *Composite Fibers* primarily consists of single-serve coffee and tea filtration papers, metallized and self adhesive labeling papers, composite laminates used for decorative furniture and flooring applications, and technical specialties such as battery pasting papers, among others; and

- *Advanced Airlaid Materials* with revenue from the sale of airlaid non-woven fabric-like materials used in feminine hygiene and adult incontinence products, cleaning pads and wipes, food pads, napkins, tablecloths, and baby wipes.

The markets served by the Composite Fibers and Advance Airlaid Materials business units are characterized by attractive growth rates as the result of new and emerging products and markets, changing end-user preferences and evolving demographics. Specialty Papers serves more mature market segments, many of which are in decline.

As a result of our strategy to diversify sources of revenue and invest in growth businesses, revenue generated from Composite Fibers and Advanced Airlaid Materials is expected to represent an increasingly greater proportion of total revenue. For 2012, these two business units comprised 43% of consolidated revenue compared with 30% in 2006.

Consolidated net sales and the relative net sales contribution of each of our business units for the past three years are summarized below:

| *Dollars in thousands* | **2012** | 2011 | 2010 |
|---|---|---|---|
| Net sales | **$ 1,577,788** | $ 1,603,154 | $ 1,455,331 |
| *Business unit contribution* | | | |
| Specialty Papers | **56.7%** | 54.6% | 57.9% |
| Composite Fibers | **27.7** | 29.7 | 28.8 |
| Advanced Airlaid Materials | **15.6** | 15.7 | 13.3 |
| Total | **100.0%** | 100.0% | 100.0% |

Our strategies are focused on growing revenues, in part, by leveraging leading positions in key global growth markets including the single-serve coffee and tea markets and the hygiene products markets. To ensure we are best positioned to serve these markets, we have made investments to increase production capacity and intend to make additional future investments.

In addition to leveraging our leading positions, our focus on product innovation is a critical component of our business strategy. During 2012, 2011 and 2010, we invested $10.9 million, $11.7 million and $10.4 million, respectively, in new product development activities. In each of the past three years, in excess of 50% of net sales were generated from products developed, enhanced or improved within the past five years.

Other key elements to our success include margin expansion, driven by cost reduction and continuous improvement initiatives; the generation of strong and reliable cash flows; and strategic investments to improve our returns on invested capital. The strength of our balance sheet and generation of cash flows has allowed us to pursue strategic actions such as the $50 million investment to expand capacity in Composite Fibers and share repurchase programs executed in 2011 and 2012. Under the programs we have repurchased $54 million of our common stock. These actions and our disciplined approach to capital expenditures has resulted in the generation of returns on invested capital that exceed our cost of capital.

Table of Contents

We have a demonstrated ability to establish leading market positions through the successful acquisition and integration of complementary businesses. Since 2006, we have successfully completed and integrated four acquisitions. Our acquisition strategy complements our long-term strategy of driving growth in our markets.

**Our Business Units** We manage our company as three distinct business units: (i) Specialty Papers (ii) Composite Fibers; and (iii) Advanced Airlaid Materials. Net tons sold by each business unit for the past three years were as follows:

| *Short tons* | **2012** | 2011 | 2010 |
|---|---|---|---|
| Specialty Papers | **789,201** | 779,647 | 764,670 |
| Composite Fibers | **90,300** | 93,317 | 90,350 |
| Advanced Airlaid Materials | **90,332** | 87,951 | 72,833 |
| Total | **969,833** | 960,915 | 927,853 |

***Specialty Papers*** Our North America-based Specialty Papers business unit focuses on producing papers for the following markets:

**Carbonless & forms** papers for credit card receipts, multi-part forms, security papers and other end-user applications;

**Book publishing** papers for the production of high quality hardbound books and other book publishing needs;

**Envelope and converting** papers for the direct mail market, shopping bags, and other converting applications; and

**Engineered products** for digital imaging, casting, release, transfer, playing card, postal, FDA-compliant food and beverage applications, and other niche specialty applications.

The market segments in which Specialty Papers competes have undergone significant changes over the past several years in response to capacity exceeding demand. This business unit produces both commodity products (comprised of envelopes and certain forms) and higher-value-added specialty products.

Specialty Papers revenue composition by market consisted of the following for the years indicated:

| *In thousands* | **2012** | 2011 | 2010 |
|---|---|---|---|
| Carbonless & forms | **$ 372,950** | $ 368,582 | $ 359,033 |
| Book publishing | **155,925** | 166,506 | 168,155 |
| Envelope & converting | **174,781** | 170,380 | 157,202 |
| Engineered products | **187,724** | 166,660 | 155,257 |
| Other | **3,397** | 2,950 | 2,967 |
| Total | **$ 894,777** | $ 875,078 | $ 842,614 |

Although many of the markets served by Specialty Papers are mature and, in many instances, declining, we have been successful at maintaining this unit s shipments through new product and new business development initiatives while leveraging the flexibility of our operating assets to efficiently respond to changing customer demands. In each of the past eight years, our flexible asset base, new product development capabilities and superior customer service offerings allowed us to outperform the broader uncoated free sheet market in terms of shipping volumes.

We believe we are one of the leading suppliers of carbonless and book publishing papers in the United States. Although the markets for these products are declining, we have been successful in executing our strategy to replace this lost volume with products such as envelope papers and business forms, and other value-added specialty products. Specialty Papers also produces paper that is converted into specialized envelopes in a wide array of colors, finishes and end-uses. While this market is also declining, we have leveraged our customer service capabilities to grow our market share in each of the last several years.

Specialty Papers highly technical engineered products include those designed for multiple end uses, such as papers for pressure-sensitive postage stamps, greeting and playing cards, conical cups, digital imaging applications and for release paper applications. Such products comprise an array of distinct business niches that are in a continuous state of evolution. Many of these products are utilized for demanding, specialized customer and end-user applications. Some of our products are new and higher growth while others are more mature and further along in the product life cycle. Because many of these products are technically complex and involve substantial customer-supplier development collaboration, they typically command higher per ton prices and generally exhibit greater pricing stability relative to commodity grade paper products.

The Specialty Papers business unit operates two integrated pulp and paper making facilities with the following combined attributes:

| Uncoated Production Capacity (short tons) | Principal Raw Material ( PRM ) | Estimated Annual Quantity of PRM (short tons) |
|---|---|---|
| 795,000 | Pulpwood | 2,327,250 |
| | Wood-and other pulps | 721,600 |

This business unit s pulp mills have a combined pulp making capacity of 598,000 tons of bleached pulp per year. The principal raw material used to produce each

2

Table of Contents

facility s pulp is pulpwood, including both hardwoods and softwoods. Pulpwood is obtained from a variety of locations including the states of Pennsylvania, Maryland, Delaware, New Jersey, New York, West Virginia, Virginia, Kentucky, Ohio and Tennessee. To protect our sources of pulpwood, we actively promote conservation and forest management among suppliers and woodland owners. In addition to critical raw materials, the cost to produce Specialty Papers products is influenced by energy costs. Although the business unit generates all of its steam needed for production at both facilities and generates more power than it consumes at the Spring Grove, PA facility, in 2012, it purchased approximately 22% of its electricity needed for the Chillicothe, OH mill. The facilities source of fuel is primarily coal and, to a lesser extent, natural gas.

Since becoming a member of PJM Interconnection, a federally regulated Independent System Operator ( ISO ) that coordinates the movement and ensures reliability of wholesale electricity in its region, excess electricity generated by Spring Grove is sold to the high-voltage electricity grid. As a member of PJM, we provide capacity to the grid and sell excess power at market prices. Accordingly, our margin earned from energy sales will be subject to market volatility associated with the price at which energy is sold together with volatility in input costs, primarily related to coal.

The Spring Grove facility includes five uncoated paper machines as well as an off-line combi-blade coater and a Specialty Coater ( S-Coater ), which together provide annual production capacity for coated paper of approximately 68,000 tons. Since uncoated paper is used in producing coated paper, this is not additional capacity. The Chillicothe facility operates four paper machines producing uncoated and carbonless paper. Two of the machines have built-in coating capability which along with three additional coaters at the facility provide annual coated capacity of 130,000 tons.

In the carbonless paper market, we compete with Appleton Papers and, to a lesser extent, foreign importers including Fibria Celulose (formerly Votorantim Celulose e Papel) and Asia Pulp and Paper Co. We believe we are one of the leading producers of book publishing papers and compete in these markets with Domtar Corp. and North Pacific Paper (NORPAC), among others. In the envelope sector we compete with International Paper, Domtar Corp., Boise Inc. and Evergreen Packaging, among others. In our Specialty Papers engineered products markets, competition is product line specific as the necessity for technical expertise and specialized manufacturing equipment limits the number of companies offering

multiple product lines. We compete with specialty divisions of large companies such as International Paper, Domtar Corp., Boise Inc., NewPage Corp. and Sappi Limited, among others. Service, product performance, technological advances and product pricing are important competitive factors with respect to all our products. We believe our reputation in these areas continues to be excellent.

To be successful in the market environment in which Specialty Papers operates, our strategy is focused on:

- employing our new product and new business development capabilities to meet changing customer demands and ensure optimal utilization of capacity;
- leveraging our flexible operating platform to optimize product mix by shifting production among facilities to more closely match output with changing demand trends;
- aggressively employing methodologies to manage pressures on margins presented by more mature markets;
- utilizing ongoing continuous improvement methodologies to ensure operational efficiencies; and
- maintaining superior customer service.

***Composite Fibers*** Our Composite Fibers business unit, based in Gernsbach, Germany, serves customers globally and focuses on higher value-added products in the following markets:

**Food & Beverage** paper primarily used for single-serve coffee and tea products;

**Metallized** products used in the labeling of beer bottles, packaging innerliners, gift wrap, self-adhesive labels and other consumer product applications;

**Composite Laminates** papers used in production of decorative laminates, furniture, and flooring applications; and

**Technical Specialties** a diverse line of paper products used in batteries, adhesive tapes and other highly-engineered applications.
We believe this business unit maintains a market leadership position in the single-serve coffee and tea markets, and the composite laminates market. Composite

Table of Contents

Fibers revenue composition by market consisted of the following for the years indicated:

| *In thousands* | **2012** | 2011 | 2010 |
|---|---|---|---|
| Food & beverage | **$ 265,423** | $ 284,748 | $ 242,882 |
| Metallized | **87,720** | 95,276 | 88,753 |
| Composite laminates | **44,613** | 53,334 | 50,801 |
| Technical specialties and other | **38,984** | 42,671 | 36,781 |
| Total | **$ 436,740** | $ 476,029 | $ 419,217 |

We believe many of the market segments served by Composite Fibers, particularly single-serve coffee and tea, present attractive growth opportunities by capitalizing on evolving consumer preferences, expanding into new or emerging geographic markets, and by gaining market share through quality product and service offerings. Many of this unit s papers are technically sophisticated and most, except for metallized papers, are extremely lightweight and require specialized fibers. Our engineering capabilities, specifically designed papermaking equipment, use of specialized fibers and customer orientation positions us well to compete in these global markets.

The primary raw materials used in the production of our lightweight papers are abaca pulp and wood pulp. Abaca pulp is a specialized pulp with limited sources of availability. Our abaca pulp production process, fulfilled by our Philippine mill, provides a unique advantage by supplying a key raw material used by our Composite Fibers business unit. Sufficient quantities of abaca pulp and the source fiber are required to support growth in this business unit. In the event the supply of abaca fiber becomes constrained or when production demands exceed the capacity of the Philippines mill, alternative sources and/or substitute fibers are used to meet customer demands.

The Composite Fibers business unit is comprised of three paper making facilities (Germany, France and England), metallizing operations (Wales and Germany) and a pulp mill (the Philippines) with the following combined attributes:

| Production Capacity (short tons) | Principal Raw Material ( PRM ) | Estimated Annual Quantity of PRM (short tons) |
|---|---|---|
| 68,400 lightweight | Abaca pulp | 18,100 |
| | Wood pulp | 46,000 |
| | Synthetic fiber | 12,800 |
| 28,100 metallized | Base stock | 30,200 |
| 15,300 abaca pulp | Abaca fiber | 26,270 |

Composite Fibers uses highly specialized inclined wire paper machine technology and we believe we currently maintain approximately 25% of the global inclined wire capacity.

In addition to critical raw materials, the cost to produce Composite Fibers products is influenced by energy costs. Although the business unit generates all of its steam needed for production, in 2012, it purchased 93% of its electricity.

In Composite Fibers markets, competition is product line specific as the necessity for technical expertise and specialized manufacturing equipment limits the number of companies offering multiple product lines. In single-serve coffee and tea products we compete with companies such as Ahlstrom and Purico. In composite laminates, we compete with PdM, a division of Schweitzer-Maudit, Purico, MB Papeles and Oi feng. For metallized products, competitors include AR Metallizing, Torras Papel Novelis, Vaassen, and Wenzhou Protec Vacuum Metallizing Co. Ltd.

Our strategy in Composite Fibers is focused on:

- capturing global growth in food & beverage, technical specialties and composite laminates;

- expanding value-added production capacity by investing in state-of-the-art inclined wire technology to better ensure our capacity supports consistent growth of markets;
- capitalizing on rapidly growing markets;
- enhancing product mix across all of the business unit s markets by utilizing new product and new business development capabilities;
- implementing continuous improvement methodologies to increase productivity, reduce costs and expand capacity; and
- ensuring readily available access to specialized raw material requirements to support projected growth.

As part of our commitment to realizing the growth potential of certain of this business unit s markets, we announced a $50 million investment to expand our inclined wire capacity by nearly 20%, or approximately 10,500 short tons, by converting a flat wire machine, currently producing composite laminates, to a state-of-the-art inclined wire machine. The project began in 2012 and is expected to be completed in the second quarter of 2013. Production of saleable products from the new machine is scheduled to begin in the second quarter of 2013. We expect to achieve a 15% to 20% after-tax return on this investment within three years.

***Advanced Airlaid Materials*** was formed in connection with our February 2010 acquisition of Concert Industries Corp. ( Concert ). Advanced Airlaid Materials is

4

Table of Contents

a leading global supplier of highly absorbent cellulose-based airlaid non-woven materials used to manufacture consumer and industrial products for growing global end-user markets. These products include, but are not limited to:

feminine hygiene;

adult incontinence;

home care;

specialty wipes;

table top; and

food pads.

Advanced Airlaid Materials affords us the opportunity to grow with customers who are industry leading consumer product companies for feminine hygiene and adult incontinence products. Advanced Airlaid Materials holds leading market share positions in many of the markets it serves, excels in building long-term customer relationships through superior quality and customer service programs, and has a well-earned reputation for innovation and its ability to quickly bring new products to market.

Advanced Airlaid Materials revenue composition by market consisted of the following for the years indicated:

| *In thousands* | **2012** | 2011 | 2010 |
|---|---|---|---|
| Feminine hygiene | **$ 197,792** | $ 206,724 | $ 157,660 |
| Home care | **14,527** | 15,308 | 13,691 |
| Wipes | **13,562** | 5,463 | |
| Adult incontinence | **6,959** | 6,083 | 6,167 |
| Other | **13,442** | 18,469 | 15,981 |
| Total | **$ 246,282** | $ 252,047 | $ 193,499 |

The feminine hygiene category accounted for 80% of Advanced Airlaid Material s revenue in 2012, sales of which are to a small group of large, leading global consumer products companies. This market is considered to be more growth oriented driven by population growth in certain geographic regions, consumer preferences, and suppliers ability to provide innovative products. In developing regions, demand is also influenced by increases in disposable income and cultural preferences.

The Advanced Airlaid Materials business unit operates state-of-the-art facilities in Falkenhagen, Brandenburg, Germany and Gatineau, Quebec, Canada. The Falkenhagen location operates three multi-bonded production lines and three proprietary single-lane festooners. The Gatineau location consists of two airlaid production lines employing multi-bonded and thermal-bonded airlaid technologies and, with the recently completed investment, two proprietary single-lane festooners.

The business unit s two facilities operate with the following combined attributes:

| Airlaid Production Capacity (short tons) | Principal Raw Material ( PRM ) | Estimated Annual Quantity of PRM (short tons) |
|---|---|---|

| | | |
|---|---|---|
| 107,000 | Fluff pulp | 73,250 |

In addition to the cost of critical raw materials, the cost to produce multi-bonded and thermal-bonded airlaid materials is impacted by energy costs. Advanced Airlaid Materials purchases all of its electricity and natural gas. Approximately 80% of this business unit s revenue is earned under contracts with pass-through provisions directly related to the price of key input costs.

Advanced Airlaid Materials continues to be a technology and product innovation leader in technically demanding segments of the airlaid market, most notably feminine hygiene. We believe that its facilities are among the most modern and flexible airlaid facilities in the world, allowing it to produce at industry leading operating rates. Its proprietary single-lane rotary festooning technology, developed in 2002, provides customers with a product packaged for efficient use. This business unit s in-house technical expertise, combined with significant capital investment requirements and rigorous customer expectations creates large barriers to entry for new competitors.

The airlaid industry is made up of several producers, including Buckeye Technologies Inc., Georgia-Pacific LLC, Duni AB, Petropar SA, McAirlaid s Vliestoffe GmbH & Co. KG, and us.

The markets served by this business unit are characterized by attractive growth opportunities. To take advantage of this, our strategy is focused on:

- maintaining and expanding relationships with customers that are market-leading consumer product companies;
- expanding geographic reach of markets served;
- optimizing the use of existing production capacity;
- employing continuous improvement methodologies and initiatives to reduce costs, improve efficiencies and create capacity; and
- capitalizing on our product and process innovation capabilities.

Additional financial information for each of our business units is included in Item 7 Management s Discussion and Analysis of Financial Condition and Results of Operations and in Item 8 Financial Statements and Supplementary Data, Note 22 including geographic revenue and long-lived asset financial information.

Table of Contents

**Balance Sheet** We are focused on prudent financial management and the maintenance of a conservative capital structure and strong balance sheet. This includes:

- aggressively managing working capital to enhance cash flow from operations;
- making disciplined capital expenditure decisions; and
- monetizing the value of our timberland assets as opportunities develop.

The success of these actions positions us with the flexibility to pursue strategic opportunities that will benefit our shareholders.

**Concentration of Customers** For each of the past three years, no single customer represented more than 10% of our consolidated net sales. However, as discussed in Item 1A Risk Factors, one customer accounted for the majority of Advanced Airlaid Materials net sales in 2012, 2011 and 2010.

**Capital Expenditures** Our business is capital intensive and requires extensive expenditures for new and enhanced equipment. These capital investments are necessary to support growth strategies, research and development initiatives, environmental compliance, and for normal upgrades or replacements. Capital expenditures totaled $58.8 million, $64.5 million and $36.5 million, in 2012, 2011 and 2010, respectively. For 2013, capital expenditures are estimated to be $90 million to $100 million. This includes $33.5 million of the $50 million investment to expand capacity to serve Composite Fibers growth markets.

**Environmental Matters** We are subject to various federal, state and local laws and regulations intended to protect the environment as well as human health and safety. At various times, we have incurred significant costs to comply with these regulations and we could incur additional costs as new regulations are developed or regulatory priorities change. As a result of new air quality regulations including the U.S. EPA Best Available Retrofit Technology rule (BART; otherwise known as the Regional Haze Rule) and the Boiler Maximum Achievable Control Technology rule (Boiler MACT), we anticipate that we could incur material capital and operating costs. For example, on December 20, 2012, the Administrator of the U. S. Environmental Protection Agency signed new rules which could require process modifications and/or installation of air pollution controls on power boilers at two of our facilities. We are currently reviewing these rules to understand the effect they may have on our

operations, such as reducing or curtailing boiler usage or modifying the types of boilers operated or fuel consumed. The cost of compliance is likely to be significant. Our current estimates to implement viable options could result in additional capital spending of approximately $45 million. The amount ultimately incurred may be less depending on our successful implementation of appropriate available options. In addition, the timing of any additional capital spending is uncertain, although we currently expect to incur the expenditures generally in 2015 and 2016. Enactment of new environmental laws or regulations or changes in existing laws or regulations could significantly change our estimates. For a discussion of other environmental matters, see Item 8 Financial Statements and Supplementary Data Note 21.

**Employees** As of December 31, 2012, we employed 4,258 people worldwide, of which approximately 70% are unionized. The United Steelworkers International Union and the Office and Professional Employees International Union represents approximately 1,600 hourly employees at our Chillicothe, OH and Spring Grove, PA facilities under labor contracts expiring in November 2015 and January 2014, respectively. Hourly employees at each of our international locations are represented by various unions or works councils. We consider the overall relationship with our employees to be satisfactory.

**Other Available Information** The Corporate Governance page of our corporate web site includes our Governance Principles and Code of Business Conduct, and biographies of our Board of Directors and Executive Officers. In addition, the website includes the charters for the Audit, Compensation, Finance, and Nominating and Corporate Governance Committees of the Board of Directors. The Corporate Governance page also includes the Code of Business Ethics for the CEO and Senior Financial Officers of Glatfelter, our whistle-blower policy and other related material. We satisfy the disclosure requirement for any future amendments to, or waivers from, our Code of Business Conduct or Code of Business Ethics for the CEO and Senior Financial Officers by posting such information on our website. We will provide a copy of the Code of Business Conduct or Code of Business Ethics for the CEO and Senior Financial Officers, without charge, to any person who requests one, by contacting Investor Relations at (717) 225-2719, ir@glatfelter.com or by mail to 96 South George Street, Suite 520, York, PA, 17401.

**Table of Contents**

***ITEM 1A RISK FACTORS***
***Our business and financial performance may be adversely affected by the global economic environment or downturns in the target markets that we serve.***

Adverse global economic conditions could impact our target markets resulting in decreased demand for our products. Approximately 17% of our net sales in 2012 were shipped to customers in western Europe, the demand for which, in many cases, is dependent on economic conditions in this area, and to the extent customers do business outside of Europe, in other regions of the world. Our results could be adversely affected if economic conditions weaken or fail to improve. Also, there may be periods during which demand for our products is insufficient to enable us to operate our production facilities in an economical manner. The economic environment may cause customer insolvencies which may result in their inability to satisfy their financial obligations to us. These conditions are beyond our ability to control and may have a significant impact on our sales and results of operations.

The markets for our products are also significantly affected by changes in industry capacity and output. There have been periods of supply/demand imbalance in our industry which have caused pulp prices and our products selling prices to be volatile. The timing and magnitude of price increases or decreases in these markets have generally varied by region and by product type. A sustained period of weak demand or excess supply would likely adversely affect pulp prices and our products selling prices. This could have a material adverse affect on our operating and financial results.

***The cost of raw materials and energy used to manufacture our products could increase and the availability of certain raw materials could become constrained.***

We require access to sufficient and reasonably priced quantities of pulpwood, purchased pulps, pulp substitutes, abaca fiber, synthetic fibers, and certain other raw materials. Our Spring Grove and Chillicothe locations are vertically integrated manufacturing facilities that generate approximately 82% of their annual pulp requirements.

Our Philippine mill purchases abaca fiber to produce abaca pulp, which we use to manufacture our paper for single-serve coffee, tea and technical specialty products at our Gernsbach, Scaër and Lydney facilities. At certain times in the past, the supply of abaca fiber has been constrained due to factors such as weather related damage to the

source crop as well as decisions by land owners to produce alternative crops in lieu of those used to produce abaca fiber.

Our Advanced Airlaid Materials business unit requires access to sufficient quantities of fluff pulp, the supply of which is subject to availability of certain softwoods. Softwood availability can be limited by many factors, including weather in regions where softwoods are abundant.

The cost of many of our production materials, including petroleum based chemicals, and freight charges, are influenced by the cost of oil. In addition, coal is a principal source of fuel for both the Spring Grove and Chillicothe facilities and natural gas is used as a source of fuel for our Chillicothe facility, and the Composite Fibers and Advanced Airlaid Materials business units facilities.

Although we have contractual cost pass-through arrangements with certain customers, we may not be able to fully pass increased raw materials or energy costs on to all customers if the market will not bear the higher price or where existing agreements with our customers limit price increases. If price adjustments significantly trail increases in raw materials or energy prices, our operating results could be adversely affected.

***Our industry is highly competitive and increased competition could reduce our sales and profitability.***

In the past, global industries in which we compete have been adversely affected by capacity exceeding the demand for products and by declining uncoated free sheet demand. As a result, steps have been taken to reduce underperforming capacity. However, slowing demand or increased competition could force us to lower our prices or to offer additional services at a higher cost to us, which could reduce our gross margins and net income. The greater financial resources of certain of our competitors may enable them to commit larger amounts of capital in response to changing market conditions. Certain competitors may also have the ability to develop product or service innovations that could put us at a competitive disadvantage.

Some of the factors that may adversely affect our ability to compete in the markets in which we participate include:

- the entry of new competitors into the markets we serve, including foreign producers;

- the willingness of commodity-based producers to enter our markets when they are unable to compete or when demand softens in their traditional markets;

Table of Contents

- the aggressiveness of our competitors pricing strategies, which could force us to decrease prices in order to maintain market share;
- our failure to anticipate and respond to changing customer preferences;
- the impact of electronic-based substitutes for certain of our products such as carbonless and forms, book publishing, and envelope papers;
- the impact of replacement or disruptive technologies;
- changes in end-user preferences;
- our inability to develop new, improved or enhanced products; and
- our inability to maintain the cost efficiency of our facilities.

If we cannot effectively compete in the markets in which we operate, our sales and operating results would be adversely affected.

***We may not be able to develop new products acceptable to our customers.***

Our business strategy is market focused and includes investments in developing new products to meet the changing needs of our customers and to maintain our market share. Our success will depend, in part on our ability to develop and introduce new and enhanced products that keep pace with introductions by our competitors and changing customer preferences. If we fail to anticipate or respond adequately to these factors, we may lose opportunities for business with both current and potential customers. The success of our new product offerings will depend on several factors, including our ability to:

- anticipate and properly identify our customers needs and industry trends;
- price our products competitively;
- develop and commercialize new products and applications in a timely manner;
- differentiate our products from our competitors products; and
- invest efficiently in research and development activities.

Our inability to develop new products could adversely impact our business and ultimately harm our profitability.

***We are subject to substantial costs and potential liability for environmental matters.***

We are subject to various environmental laws and regulations that govern our operations, including discharges into the environment, and the handling and disposal of hazardous substances and wastes. We are also subject to laws and regulations that impose liability and clean-up responsibility for releases of hazardous substances into the environment. The Clean Air Act, and similar regulations, could impose significant compliance costs or require significant capital expenditures. To comply with environmental laws and regulations, we have incurred, and will continue to incur, substantial capital and operating expenditures. We anticipate that environmental regulation of our operations will continue to become more burdensome and that capital and operating expenditures necessary to comply with environmental regulations will continue, and perhaps increase, in the future. Because environmental regulations are not consistent worldwide, our ability to compete globally may be adversely affected by capital and operating expenditures required for environmental compliance. In addition, we may incur obligations to remove or mitigate any adverse effects on the environment, such as air and water quality, resulting from mills we operate or have operated. Potential obligations include compensation for the restoration of natural resources, personal injury and property damages.

Despite favorable rulings in the pending Fox River litigation, we continue to have exposure to liability for remediation and other costs related to the presence of polychlorinated biphenyls in the lower Fox River on which our former Neenah, Wisconsin mill was located. There can be no assurance that we will not be required to ultimately pay material amounts to resolve our liability in the Fox River matter. We have financial reserves for environmental matters, including the Fox River site, but we cannot be certain that those reserves will be adequate to provide for future obligations related to these matters, that our share of costs and/or damages for these matters will not exceed our available resources, or that such obligations will not have a long-term, material adverse effect on our consolidated financial position, liquidity or results of operations.

Our environmental issues are complex and should be reviewed in the context set forth in more detail in Item 8 Financial Statements and Supplementary Data Note 21.

Table of Contents

***The Advanced Airlaid Materials business unit generates a substantial portion of its revenue from one customer serving the hygiene products market, the loss of which could have a material adverse effect on our results of operations.***

Advanced Airlaid Materials generates the majority of its net sales of hygiene products from one customer. The loss of this significant customer could have a material adverse effect on their operating results. In addition, sales in the feminine hygiene market accounted for 80% of Advanced Airlaid Materials net sales in 2012 and sales are concentrated within a small group of large customers. A decline in sales of hygiene products could have a material adverse effect on this unit s operating results. Customers in the airlaid non-woven fabric material market, including the hygiene market, may also switch to less expensive products, change preferences or otherwise reduce demand for Advanced Airlaid Material s products, thus reducing the size of the markets in which it currently sells its products. Any of the foregoing could have a material adverse effect on our financial performance and business prospects.

***Our operations may be impaired and we may be exposed to potential losses and liability as a result of natural disasters, acts of terrorism or sabotage or similar events.***

If we have a catastrophic loss or unforeseen operational problem at certain of our facilities, we could suffer significant lost production which could impair our ability to satisfy customer demands.

Natural disasters, such as earthquakes, flooding or fire, and acts of terrorism or sabotage affecting our operating activities and major facilities could materially and adversely affect our operations, operating results and financial condition. In addition, we own and maintain four dams in York County, Pennsylvania, that were built to ensure a steady supply of water for the operation of our facility in Spring Grove which is a primary manufacturing location for our envelope papers and engineered products. Each of these dams is classified as high hazard by the Commonwealth of Pennsylvania because they are located in close proximity to inhabited areas. Any sudden failure of a dam, including as a result of natural disaster or act of terrorism or sabotage, would endanger occupants and residential, commercial and industrial structures, for which we could be liable. The failure of a dam could also be extremely disruptive and result in damage to or the shutdown of our Spring Grove mill. Any losses or liabilities incurred due to the failure of one of our dams may not be fully covered by our insurance policies or may substantially exceed the limits of our

policies, and could materially and adversely affect our operating results and financial condition.

In addition, many of our papermaking operations require a reliable and abundant supply of water. Such mills rely on a local water body or water source for their water needs and, therefore, are particularly impacted by drought conditions or other natural or manmade interruptions to its water supplies. At various times and for differing periods, each of our mills has had to modify operations due to water shortages, water clarity, or low flow conditions in its principal water supplies. Any interruption or curtailment of operations at any of our paper mills due to drought or low flow conditions at the principal water source or another cause could materially and adversely affect our operating results and financial condition.

Our pulp mill in Lanao del Norte on the Island of Mindanao in the Republic of the Philippines is located along the Pacific Rim, one of the world s hazard belts. By virtue of its geographic location, this mill is subject to, among similar types of natural disasters discussed above, cyclones, typhoons, and volcanic activity. Moreover, the area of Lanao del Norte has been a target of suspected terrorist activities. The most common bomb targets in Lanao del Norte to date have been power transmission towers. Our pulp mill in Mindanao is located in a rural portion of the island and is susceptible to attacks or power interruptions. The Mindanao mill supplies approximately 85% of the abaca pulp that is used by our Composite Fibers business unit to manufacture our paper for single serve coffee and tea products and certain technical specialties products. Any interruption, loss or extended curtailment of operations at our Mindanao mill could materially affect our operating results and financial condition.

***We have operations in a potentially politically and economically unstable location.***

Our pulp mill in the Philippines is located in a region that is unstable and subject to political unrest. As discussed above, our Philippine pulp mill produces abaca pulp, a significant raw material used by our Composite Fibers business unit, and is currently our main provider of abaca pulp. There are limited suitable alternative sources of readily available abaca pulp in the world. In the event of a disruption in supply from our Philippine mill, there is no guarantee that we could obtain adequate amounts of abaca pulp from alternative sources at a reasonable price or at all. As a consequence, any civil disturbance, unrest, political instability or other event that causes a disruption in supply could limit the availability of abaca pulp and would increase our cost of obtaining abaca pulp. Such occurrences could adversely impact our sales volumes, revenues and operating results.

Table of Contents

***Our international operations pose certain risks that may adversely impact sales and earnings.***

We have significant operations and assets located in Canada, Germany, France, the United Kingdom, and the Philippines. Our international sales and operations are subject to a number of unique risks, in addition to the risks in our domestic sales and operations, including differing protections of intellectual property, trade barriers, labor unrest, exchange controls, regional economic uncertainty, differing (and possibly more stringent) labor regulation, risk of governmental expropriation, domestic and foreign customs and tariffs, differing regulatory environments, difficulty in managing widespread operations and political instability. These factors may adversely affect our future profits. Also, in some foreign jurisdictions, we may be subject to laws limiting the right and ability of entities organized or operating therein to pay dividends or remit earnings to affiliated companies unless specified conditions are met. Any such limitations would restrict our flexibility in using funds generated in those jurisdictions.

***Foreign currency exchange rate fluctuations could adversely affect our results of operations.***

As we diversify our business and expand our global footprint, an increasing proportion of our revenue is generated outside of the United States. We also own and operate manufacturing facilities in Canada, Germany, France, the United Kingdom and the Philippines. Currently, the majority of our business is transacted in U.S. dollars; however, an increasing portion of business is transacted in Euros, British Pound Sterling, Canadian dollars or Philippine Peso. With respect to the Euro, we generate substantially greater cash inflow in this currency than we do outflow. However, with respect to the British Pound Sterling, Canadian dollar, and Philippine Peso, we have greater outflows than inflows of these currencies. As a result of these positions, we are exposed to changes in currency exchange rates. Uncertainty with respect to the ability of certain European countries to continue to service their sovereign debt obligations and actions proposed to restructure such obligations may cause the value of the euro to fluctuate further. In the event that one or more European countries were to replace the euro with another currency, business may be adversely affected until stable exchange rates are established.

Our ability to maintain our products price competitiveness is reliant, in part, on the relative strength of the currency in which the product is denominated compared to the currency of the market into which it is sold and the functional currency of our competitors.

Changes in the rate of exchange of foreign currencies in relation to the U.S. dollar, and other currencies, may adversely impact our results of operations and our ability to offer products in certain markets at acceptable prices.

***An IRS audit of our 2009 tax return could result in a change in the tax treatment of the alternative fuel mixture credits we claimed in 2009, which could have a material adverse effect on our results of operations and financial position.***

The U.S. Internal Revenue Code, or the Code, provided a tax credit for companies that used alternative fuel mixtures to produce energy to operate their businesses on or prior to December 31, 2009. During 2009, we registered two of our facilities with the IRS as alternative fuel mixers based on their use of black liquor as an alternative fuel source. For the year ended December 31, 2009, we had substantial alternative fuel mixture credits relating to these facilities. Our results of operations in 2009 included, on a pre-tax basis, $107.8 million of alternative fuel mixture credits. During 2012, we amended our 2009 federal income tax return to convert a portion of the alternative fuel mixture credits for cellulosic biofuel production credits. In the event that the IRS audits our tax return for the year ended December 31, 2009, the IRS may conclude that some or all of the credits claimed are subject to federal income taxes, which would subject us to additional tax liabilities and could have a material adverse effect on our results of operations and financial position.

***In the event any of the above risk factors impact our business in a material way or in combination during the same period, we may be unable to generate sufficient cash flow to simultaneously fund our operations, finance capital expenditures, satisfy obligations and make dividend payments on our common stock.***

In addition to debt service obligations, our business is capital intensive and requires significant expenditures to support growth strategies, research and development initiatives, environmental compliance, and for normal upgrades or replacements. We expect to meet all of our near and long-term cash needs from a combination of operating cash flow, cash and cash equivalents, our existing credit facility and other long-term debt. If we are unable to generate sufficient cash flow from these sources, we could be unable to meet our near and long-term cash needs or make dividend payments.

Table of Contents

***ITEM 1B UNRESOLVED STAFF COMMENTS***

None.

***ITEM 2 PROPERTIES***

We own substantially all of the land and buildings comprising our manufacturing facilities located in Pennsylvania; Ohio; Canada; the United Kingdom; Germany; France; and the Philippines; as well as substantially all of the equipment used in our manufacturing and related operations. Certain of our operations, particularly our metallized paper production facility located in Caerphilly, Wales, office and warehouse space in Moscow, Russia and our corporate offices located in York, Pennsylvania are under lease agreements. All of our properties, other than those that are leased, are free from any material liens or encumbrances. We consider all of our buildings to be in good structural condition and well maintained and our properties to be suitable and adequate for present operations.

***ITEM 3 LEGAL PROCEEDINGS***

We are involved in various lawsuits that we consider to be ordinary and incidental to our business. The ultimate outcome of these lawsuits cannot be predicted with certainty; however, we do not expect such lawsuits, individually or in the aggregate, will have a material adverse effect on our consolidated financial position, liquidity or results of operations.

For a discussion of commitments, legal proceedings and related contingencies, see Item 8 Financial Statements and Supplementary Data Note 21.

**EXECUTIVE OFFICERS**

The following table sets forth certain information with respect to our executive officers and senior management as of March 7, 2013.

| Name | Age | Office with the Company |
|---|---|---|
| Dante C. Parrini | 48 | Chairman and Chief Executive Officer |
| John P. Jacunski | 47 | Senior Vice President and Chief Financial Officer |
| Christopher W. Astley | 40 | Vice President, Corporate Strategy |
| Jonathan A. Bourget | 48 | Vice President & General Manager, Advanced Airlaid Materials Business Unit |
| David C. Elder | 44 | Vice President, Finance |
| Debabrata Mukherjee | 43 | Vice President & General Manager, Specialty Papers Business Unit |
| Martin Rapp | 53 | Vice President & General Manager, Composite Fibers Business Unit |
| Mark A. Sullivan | 58 | Vice President, Global Supply Chain and Information Technology |
| William T. Yanavitch II | 52 | Vice President, Human Resources and Administration |

Officers are elected to serve at the pleasure of the Board of Directors. Except in the case of officers elected to fill a new position or a vacancy occurring at some other date, officers are generally elected at the organizational meeting of the Board of Directors held immediately after the annual meeting of shareholders.

**Dante C. Parrini** became Chief Executive Officer effective January 1, 2011 and Chairman of the Board in May 2011. Prior to this, he was Executive Vice President and Chief Operating Officer, a position he held since February 2005. Mr. Parrini joined us in 1997 and has previously served as Senior Vice President and General Manager, a position he held beginning in January 2003 and prior to that as Vice President responsible for Sales and Marketing.

**John P. Jacunski** became Senior Vice President and Chief Financial Officer in July 2006. From October 2003 until July 2006, he was Vice President and Corporate Controller. Mr. Jacunski was previously Vice President and Chief Financial Officer at WCI Steel, Inc. from June 1999 to October 2003. Prior to joining WCI, Mr. Jacunski was with KPMG, an international accounting and consulting firm, where he served in various capacities.

**Christopher W. Astley** joined us in August 2010 as Vice President, Corporate Strategy. He has over fifteen years experience as an advisor and practitioner leading critical strategic and tactical corporate initiatives for natural resource companies, with a focus since 1999 on the pulp, paper, and packaging industries. Mr. Astley previously held positions with Accenture, a global management consulting firm, and The Coca-Cola

Company, as well as successfully leading a privately held business for several years.

**Jonathan A. Bourget** joined us in July 2010 as Vice President & General Manager, Advanced Airlaid Materials Business Unit. From 2008 until joining our Company, Mr. Bourget was Vice President & General Manager of European operations at Polymer Group Inc. Prior to this, he held various positions of increasing responsibility, including General Manager Specialties Division in Europe, with Alcoa Inc.

**David C. Elder** was promoted to Vice President, Finance in December 2011 and continues as our Chief Accounting Officer. Prior to his promotion, he was our Vice President, Corporate Controller, a position held since joining Glatfelter in January 2006. Mr. Elder was previously Corporate Controller for YORK International Corporation and prior to that he was the Director, Financial Planning and Analysis for that company.

Table of Contents

**Debabrata Mukherjee** was appointed Vice President & General Manager, Specialty Papers Business Unit in April 2008. Dr. Mukherjee joined our Company in 1998 and since then has held various operational, sales and technical leadership positions within the Specialty Papers Business Unit. From March 2006 through March 2008, Dr. Mukherjee served as Division Vice President, Engineered & Converting Products. From February 2004 through February 2006, Dr. Mukherjee served as Director, Engineered Products. Prior to joining Glatfelter, Dr. Mukherjee served in various capacities with Felix Schoeller, a Germany based global specialty paper manufacturer.

**Martin Rapp** joined Glatfelter in August 2006 and serves as Vice President and General Manager, Composite Fibers Business Unit. Prior to this, Mr. Rapp was Vice President and General Manager of Avery Dennison s Roll Materials Business in Central and Eastern Europe since August 2002.

**Mark A. Sullivan** joined our Company in December 2003 and serves as Vice President, Global Supply Chain and Information Technology. Previously, he was our Chief Procurement Officer. Prior to joining Glatfelter, his experience included a broad array of operations and supply chain management responsibilities during twenty years with the DuPont Company.

**William T. Yanavitch II** was appointed Vice President, Human Resources and Administration in May 2005. Mr. Yanavitch briefly worked with Constellation Energy in Human Resources from February 2005 May 2005. He served as our Vice President Human Resources from July 2000 until January 2005. Prior to joining us he worked for Dentsply International and Gould Pumps Inc. in various leadership capacities.

## *ITEM 4 MINE SAFETY DISCLOSURES*

Not Applicable

## PART II

## *ITEM 5 MARKET FOR REGISTRANT S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES*

### Common Stock Prices and Dividends Declared Information

The following table shows the high and low prices of our common stock traded on the New York Stock Exchange under the symbol GLT and the dividend declared per share for each quarter during the past two years:

| Quarter | High | Low | Dividend |
|---|---|---|---|
| **2012** | | | |
| **Fourth** | **$ 18.58** | **$ 15.31** | **$ 0.09** |
| **Third** | **18.25** | **15.43** | **0.09** |
| **Second** | **16.47** | **14.25** | **0.09** |
| **First** | **16.36** | **14.12** | **0.09** |
| 2011 | | | |
| Fourth | $ 15.79 | $ 12.46 | $ 0.09 |
| Third | 16.03 | 11.73 | 0.09 |
| Second | 15.51 | 12.65 | 0.09 |
| First | 13.40 | 11.00 | 0.09 |

As of March 5, 2013, we had 1,282 shareholders of record.

### STOCK PERFORMANCE GRAPH

The following graph compares the cumulative 5-year total return of our common stock with the cumulative total returns of both a peer group and a broad market index. For the year ended December 31, 2012, we compare our stock performance to the S&P Small Cap 600 Paper Products index comprised of us, Buckeye Technologies Inc., Clearwater Paper Corp., Kapstone Paper & Packaging Corp., Neenah Paper Inc., Schweitzer-Mauduit International and Wausau Paper Corp. In addition, the chart includes a comparison to the Russell 2000, which we believe is an appropriate benchmark index for stocks such as ours.

The following graph assumes that the value of the investment in our common stock, in each index, and the peer group (including reinvestment of dividends) was $100 on December 31, 2007 and charts it through December 31, 2012.

Table of Contents

*ITEM 6 SELECTED FINANCIAL DATA*

*As of or for the year ended December 31*

| *Dollars in thousands, except per share* | **2012** | 2011 | 2010 (3) | 2009 (5) | 2008 |
|---|---|---|---|---|---|
| Net sales | **$ 1,577,788** | $ 1,603,154 | $ 1,455,331 | $ 1,184,010 | $ 1,263,850 |
| Energy and related sales, net | **7,000** | 9,344 | 10,653 | 13,332 | 9,364 |
| Total revenue | **1,584,788** | 1,612,498 | 1,465,984 | 1,197,342 | 1,273,214 |
| Reversal of (charges for) shutdown and restructuring | | | | | 856 |
| Gains on dispositions of plant, equipment and timberlands, net | **9,815** | 3,950 | 453 | 898 | 18,468 |
| Net income | **$ 59,379(1)** | $ 42,694(2) | $ 54,434(4) | $ 123,442 | $ 57,888 |
| | | | | | |
| Earnings per share | | | | | |
| Basic | **$ 1.39** | $ 0.94 | $ 1.19 | $ 2.70 | $ 1.28 |
| Diluted | **1.36** | 0.93 | 1.17 | 2.70 | 1.27 |
| | | | | | |
| Total assets | **$ 1,242,985** | $ 1,136,925 | $ 1,341,747 | $ 1,190,294 | $ 1,057,309 |
| Total debt | **250,000** | 227,000 | 333,022 | 254,583 | 313,285 |
| Shareholders equity | **539,679** | 490,404 | 552,442 | 510,704 | 342,707 |
| | | | | | |
| Cash dividends declared per common share | **0.36** | 0.36 | 0.36 | 0.36 | 0.36 |
| Depreciation, depletion and amortization | **69,500** | 69,313 | 65,839 | 61,256 | 60,611 |
| Capital expenditures | **58,752** | 64,491 | 36,491 | 26,257 | 52,469 |
| Shares outstanding | **42,784** | 42,650 | 45,976 | 45,706 | 45,434 |
| Net tons sold | **969,833** | 960,915 | 927,853 | 818,905 | 829,354 |
| Number of employees | **4,258** | 4,274 | 4,337 | 3,546 | 3,633 |

(1) During 2012, we recorded after-tax charges totaling $4.8 million related to the write-off of unamortized deferred issuance costs and the early redemption premium in connection with the refinancing of $200 million of bonds. In addition, net income includes a $4.0 million benefit from the conversion of alternative fuel mixture credits for cellulosic biofuel production credits.

(2) During 2011, we recorded after-tax charges totaling $6.1 million related to the write-off of unamortized deferred issuance costs and original issue discount and the redemption premium in connection with the early redemption of $100 million of bonds.

(3) The information set forth above for 2010 includes the financial information for Concert Industries Corp. prospectively from the February 12, 2010 acquisition date.

(4) During 2010, net income included a $23.2 million tax benefit from cellulosic biofuel production credits.

(5) During 2009, we recognized $107.8 million of alternative fuel mixture credits, all of which were recorded as a reduction to cost of products sold.

Table of Contents

***ITEM 7 MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS***

**Forward-Looking Statements** This Annual Report on Form 10-K includes forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. All statements other than statements of historical fact, including statements regarding industry prospects and future consolidated financial position or results of operations, made in this Report on Form 10-K are forward looking. We use words such as anticipates , believes , expects , future , intends and similar expressions to identify forward-looking statements. Forward-looking statements reflect management s current expectations and are inherently uncertain. Our actual results may differ significantly from such expectations. The following discussion includes forward-looking statements regarding expectations of, among others, non-cash pension expense, environmental costs, capital expenditures and liquidity, all of which are inherently difficult to predict. Although we make such statements based on assumptions that we believe to be reasonable, there can be no assurance that actual results will not differ materially from our expectations. Accordingly, we identify the following important factors, among others, which could cause our results to differ from any results that might be projected, forecasted or estimated in any such forward-looking statements:

i. variations in demand for our products including the impact of any unplanned market-related downtime, or variations in product pricing;

ii. changes in the cost or availability of raw materials we use, in particular pulpwood, pulp, pulp substitutes, caustic soda, and abaca fiber;

iii. changes in energy-related costs and commodity raw materials with an energy component;

iv. our ability to develop new, high value-added products;

v. the impact of exposure to volatile market-based pricing for sales of excess electricity;

vi. the impact of competition, both domestic and international, changes in industry production capacity, including the construction of new mills or new machines, the closing of mills and incremental changes due to capital expenditures or productivity increases;

vii. the gain or loss of significant customers and/or on-going viability of such customers;

viii. cost and other effects of environmental compliance, cleanup, damages, remediation or restoration, or personal injury or property damages related thereto, such as the costs of natural resource restoration or damages related to the presence of polychlorinated biphenyls ( PCBs ) in the lower Fox River on which our former Neenah mill was located;

ix. risks associated with our international operations, including local economic and political environments and fluctuations in currency exchange rates;

x. geopolitical events, including war and terrorism;

xi. disruptions in production and/or increased costs due to labor disputes;

xii. the impact of unfavorable outcomes of audits by various state, federal or international tax authorities;

xiii. enactment of adverse state, federal or foreign tax or other legislation or changes in government policy or regulation;

xiv. adverse results in litigation in the Fox River matter;

xv. our ability to finance, consummate and integrate acquisitions;

xvi. the cost, and successful design and construction, of the Composite Fibers capacity expansion project; and

xvii. the incurrence of unforeseen costs associated with the repair of equipment and clean-up of the Scäer facility, our ability to supply this facility s customers, and the coverage provided by insurance.

**Introduction** We manufacture a wide array of specialty papers and fiber-based engineered materials. We manage our company along three business units:

- *Specialty Papers* with revenue from the sale of carbonless papers and forms, book publishing, envelope & converting papers, and fiber-based engineered products;

- *Composite Fibers* with revenue from the sale of single-serve coffee and tea filtration papers, metallized papers, composite laminates used for decorative furniture and flooring applications, and other technical specialty papers; and

- *Advanced Airlaid Materials* with revenue from the sale of airlaid non-woven fabric-like materials used in feminine hygiene products, adult incontinence products, cleaning pads, wipes, food pads, napkins, tablecloths, and baby wipes.

Table of Contents

**Overview** For the year ended December 31, 2012, net income was $59.4 million, or $1.36 per diluted share, compared with net income of $42.7 million, or $0.93 per diluted share, in 2011. The amounts reported for 2012 include after-tax charges totaling $4.8 million incurred in connection with the refinancing of $200 million fixed-rate bonds for a new $250 million fixed-rate issuance, as well as a $4.0 million benefit from the conversion of alternative fuel mixture credits for cellulosic biofuel production credits. Results for 2011 include after-tax charges totaling $7.5 million for costs incurred to redeem $100 million of fixed-rate bonds, acquisition and integration expenses and work force efficiency actions. Reported results for both years included after-tax gains of $5.4 million and $4.2 million in 2012 and 2011, respectively, from the sales of timberlands and, in 2011, the release of tax reserves related to prior timberland sales. Unfavorable foreign currency translations affected the comparison of reported results for 2012 with 2011 by $5.7 million.

From an operating perspective, our businesses performed well during 2012 compared with 2011, evidenced by a $9.9 million, or 8.9%, increase in business unit operating income led by strong improvements from Specialty Papers and Advanced Airlaid Materials. Composite Fibers results were unfavorable in the comparison by $4.7 million.

Specialty Papers operating income totaled $67.3 million and $57.3 million for 2012 and 2011, respectively. Volumes shipped increased in the comparison to 2011 and this unit s profitability was further favorably impacted by higher selling prices and slightly lower input costs partially offset by higher spending for maintenance and other costs.

Our Composite Fibers business unit s operating income decreased to $36.1 million from $40.8 million in 2011. Volumes shipped decreased 3.2% compared to 2011 reflecting generally softer economic conditions in its market segments. Unfavorable foreign currency translations affected this unit s operating income by $3.2 million.

Advanced Airlaid Materials operating income increased $4.6 million, or 34.3%, largely reflecting lower input costs and an increase in shipping volumes. Unfavorable foreign currency translations affected this unit s operating income by $3.0 million.

During 2012, we generated significant operating cash flow of $112.8 million, and although lower than 2011, this was largely due to the year over year impact of receiving cash in 2011 compared with a net outflow of cash in 2012 related to cellulosic biofuel production and alternative fuel mixture credits.

## RESULTS OF OPERATIONS

***2012 versus 2011***

The following table sets forth summarized consolidated results of operations:

| | Year Ended December 31 | |
|---|---|---|
| *In thousands, except per share* | **2012** | 2011 |
| Net sales | **$ 1,577,788** | $ 1,603,154 |
| Gross profit | **213,649** | 206,193 |
| Operating income | **101,874** | 85,272 |
| Net income | **59,379** | 42,694 |
| Earnings per diluted share | **1.36** | 0.93 |

The consolidated results of operations for 2012 and 2011 include the following items not considered to be part of our core business operations:

| *In thousands, except per share* | After-tax Gain (loss) | Diluted EPS |
|---|---|---|
| **2012** | | |
| Early redemption of $200 million bonds | **$ (4,784)** | **$ (0.11)** |
| Conversion of alternative fuel mixture/Cellulosic biofuel credits | **4,020** | **0.09** |
| Timberland sales and related transaction costs | **5,388** | **0.12** |
| 2011 | | |
| Early redemption of $100 million bonds | $ (6,065) | (0.13) |
| Charge for workforce efficiencies | (652) | (0.01) |
| Acquisition and integration costs | (792) | (0.02) |

| | | |
|---|---|---|
| Timberland sales and related transaction costs | 4,160 | 0.09 |

During 2012, the aggregate effect of the unusual items set forth above increased earnings by $4.6 million, or $0.10 per diluted share. In 2011, the items set forth above decreased earnings by $3.3 million, or $0.07 per diluted share.

**Business Units** Results of individual business units are presented based on our management accounting practices and management structure. There is no comprehensive, authoritative body of guidance for management accounting equivalent to accounting principles generally accepted in the United States of America; therefore, the financial results of individual business units are not necessarily comparable with similar information for any other company. The management accounting process uses assumptions and allocations to measure performance of the business units. Methodologies are refined from time to time as management accounting practices are enhanced and businesses change. The costs incurred by support areas not directly aligned with the business unit are allocated primarily based on an estimated utilization of support area services or are included in Other and Unallocated in the Business Unit Performance table.

Table of Contents

Management evaluates results of operations of the business units before pension expense, alternative fuel mixture credits, debt redemption costs, restructuring related charges, certain corporate level costs, and the effects of certain asset dispositions. Management believes that this is a more meaningful representation of the operating performance of its core businesses, the

profitability of business units and the extent of cash flow generated from these core operations. Such amounts are presented under the caption Other and Unallocated. This presentation is aligned with the management and operating structure of our company. It is also on this basis that the Company s performance is evaluated internally and by the Company s Board of Directors.

**Business Unit Performance**

| Year ended December 31 | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| *In millions* | Specialty Papers | | Composite Fibers | | Advanced Airlaid Materials | | Other and Unallocated | | Total | |
| | **2012** | 2011 | **2012** | 2011 | **2012** | 2011 | **2012** | 2011 | **2012** | 2011 |
| Net sales | **$ 894.8** | $ 875.1 | **$ 436.7** | $ 476.0 | **$ 246.3** | $ 252.0 | **$** | $ | **$ 1,577.8** | $ 1,603.2 |
| Energy and related sales, net | **7.0** | 9.3 | | | | | | | **7.0** | 9.3 |
| Total revenue | **901.8** | 884.4 | **436.7** | 476.0 | **246.3** | 252.0 | | | **1,584.8** | 1,612.5 |
| Cost of products sold | **779.5** | 775.7 | **362.6** | 395.7 | **218.7** | 227.7 | **10.3** | 7.2 | **1,371.1** | 1,406.3 |
| Gross profit (loss) | **122.3** | 108.7 | **74.2** | 80.3 | **27.6** | 24.3 | **(10.4)** | (7.2) | **213.6** | 206.2 |
| SG&A | **55.0** | 51.4 | **38.1** | 39.5 | **9.6** | 10.9 | **18.9** | 23.0 | **121.6** | 124.9 |
| Gains on dispositions of plant, equipment and timberlands, net | | | | | | | **(9.8)** | (4.0) | **(9.8)** | (4.0) |
| Total operating income (loss) | **67.3** | 57.3 | **36.1** | 40.8 | **18.0** | 13.4 | **(19.5)** | (26.2) | **101.9** | 85.3 |
| Non-operating expense | | | | | | | **(22.9)** | (34.4) | **(22.9)** | (34.4) |
| Income (loss) before income taxes | **$ 67.3** | $ 57.3 | **$ 36.1** | $ 40.8 | **$ 18.0** | $ 13.4 | **$ (42.4)** | $ (60.7) | **$ 78.9** | $ 50.8 |
| **Supplementary Data** | | | | | | | | | | |
| Net tons sold *(thousands)* | **789.2** | 779.6 | **90.3** | 93.3 | **90.3** | 88.0 | | | **969.8** | 960.9 |
| Depreciation, depletion and amortization | **$ 37.4** | $ 36.0 | **$ 23.5** | $ 24.8 | **$ 8.7** | $ 8.5 | **$** | | **$ 69.5** | $ 69.3 |
| Capital expenditures | **23.1** | 31.4 | **31.4** | 22.5 | **3.9** | 10.6 | **0.3** | | **58.8** | 64.5 |

The sum of individual amounts set forth above may not agree to the consolidated financial statements included herein due to rounding.

**Sales and Costs of Products Sold**

| | Year ended December 31 | | |
|---|---|---|---|
| *In thousands* | **2012** | 2011 | Change |
| Net sales | **$ 1,577,788** | $ 1,603,154 | $ (25,366) |
| Energy and related sales net | **7,000** | 9,344 | (2,344) |
| Total revenues | **1,584,788** | 1,612,498 | (27,710) |
| Costs of products sold | **1,371,139** | 1,406,305 | (35,166) |
| Gross profit | **$ 213,649** | $ 206,193 | $ 7,456 |
| Gross profit as a percent of Net sales | **13.5%** | 12.9% | |

The following table sets forth the contribution to consolidated net sales by each business unit:

| | Year ended December 31 | |
|---|---|---|
| *Percent of Total* | **2012** | 2011 |
| **Business Unit** | | |

| | | |
|---|---|---|
| Specialty Papers | **56.7%** | 54.6% |
| Composite Fibers | **27.7** | 29.7 |
| Advanced Airlaid Material | **15.6** | 15.7 |
| Total | **100.0%** | 100.0% |

Table of Contents

Net sales for 2012 decreased $25.4 million, or 1.6%, in the comparison to 2011 and totaled $1,577.8 million. The translation of foreign currencies unfavorably impacted net sales by $35.8 million more than offsetting a $3.5 million benefit from higher selling prices. Shipping volumes were up slightly as higher shipping volumes in both Specialty Papers and Advanced Airlaid Materials were offset by softer demand in Composite Fibers related to the weak European economy.

In the Specialty Papers business unit, net sales for 2012 increased $19.7 million, or 2.3%, to $894.8 million. The increase was primarily due to a $6.5 million benefit from higher selling prices and a 1.2% increase in shipping volumes.

Specialty Papers operating income in 2012 of $67.3 million was $10.0 million higher than 2011 reflecting the benefits from higher selling prices and shipping volumes, and a $5.7 million benefit from lower raw material costs. These factors were partially offset by higher maintenance and other cost inflation as well as $2.3 million of lower energy and related sales.

We sell excess power generated by the Spring Grove, PA facility. In addition, two of our facilities are registered generators of renewable energy credits ( RECs ). The following table summarizes this activity for 2012 and 2011:

| | Year ended December 31 | | |
|---|---|---|---|
| *In thousands* | **2012** | 2011 | Change |
| Energy sales | **$ 5,284** | $ 10,992 | $ (5,708) |
| Costs to produce | **(4,187)** | (9,319) | 5,132 |
| Net | **1,097** | 1,673 | (576) |
| Renewable energy credits | **5,903** | 7,671 | (1,768) |
| Total | **$ 7,000** | $ 9,344 | $ (2,344) |

RECs represent sales of certified credits earned related to burning renewable sources of energy such as black liquor and wood waste. We sell RECs into an emerging and somewhat illiquid market. The extent and value of future revenues from REC sales is dependent on many factors outside of management s control. Therefore, we may not be able to generate consistent amounts of sales of RECs in future periods.

In Composite Fibers, net sales were $436.7 million, a decrease of $39.3 million, or 8.3%, primarily due to the translation of foreign currencies which unfavorably impacted the comparison by $24.4 million. Average selling prices were essentially unchanged and total shipping volumes were lower in the comparison by 3.2%.

Composite Fibers operating income in 2012 totaled $36.1 million, a $4.7 million decrease compared to 2011 primarily due to lower shipping volumes and a $3.2 million unfavorable effect from foreign currency translation.

On October 14, 2012, a fire was sustained by our Scäer, France facility, one of several facilities within the Composite Fibers business unit. The fire damaged the electrical system primarily servicing one of two papermaking machines at the facility as well as certain mill infrastructure. All customer orders were fulfilled by shipping products on hand or by utilizing assets at the business unit s other facilities. The total cost of the fire in 2012 was $3.9 million which was offset by expected insurance recoveries, net of deductibles, of which $0.8 million was received in 2012 and the remainder is expected to be received in 2013.

In Advanced Airlaid Materials, net sales declined $5.7 million in the comparison of 2012 to 2011. The decline in net sales was due to the $11.5 million negative effect of foreign currency translation and a $2.7 million impact of lower selling prices. These factors were partially offset by the benefit from a 2.6% increase in shipping volumes.

Operating income in this business unit increased $4.6 million in 2012 compared to 2011 led by a $8.3 million benefit from lower raw material and energy costs in addition to continuous improvement initiatives including supply chain efficiencies, waste reduction and improved throughput, and benefits from a new festooner. The translation of foreign currencies negatively impacted operating income by $3.0 million.

**Pension Expense** The following table summarizes the amounts of pension expense recognized for 2012 compared to 2011:

Year ended December 31

| *In thousands* | **2012** | 2011 | Change |
|---|---|---|---|
| Recorded as: | | | |
| Costs of products sold | **$ 9,148** | $ 6,735 | $ 2,413 |
| SG&A expense | **2,467** | 3,645 | (1,178) |
| Total | **$ 11,615** | $ 10,380 | $ 1,235 |

The amount set forth above for pension expense recorded as selling, general and administrative ( SG&A ) expense in 2011 includes a $2.0 million one-time pension settlement charge recorded in connection with the retirement of our former Chief Executive Officer.

The amount of pension expense recognized each year is dependent on various actuarial assumptions and certain other factors, including discount rates and the fair value of our pension assets. Pension expense in 2013 is expected to be approximately $15.7 million due to lower discount rates and the amortization of actuarial losses.

**Gain on Sales of Plant, Equipment and Timberlands, net** During the years ended December 31, 2012 and 2011, we completed the following sales of assets:

| *Dollars in thousands* | Acres | Proceeds | Gain |
|---|---|---|---|
| **2012** | | | |
| Timberlands | **4,830** | **$ 9,494** | **$ 9,203** |
| Other | **n/a** | **778** | **612** |
| Total | | **$ 10,272** | **$ 9,815** |
| 2011 | | | |
| Timberlands | 942 | $ 3,821 | $ 3,590 |
| Other | n/a | 670 | 360 |
| Total | | $ 4,491 | $ 3,950 |

In connection with each of the asset sales set forth above, we received cash proceeds.

**Other and Unallocated** The amount of net operating expenses not allocated to a business unit and reported as Other and Unallocated in our table of *Business Unit Performance,* excluding gains from sales of plant, equipment and timberlands, totaled $29.3 million in 2012 compared with $30.2 million in 2011. The amount reported for 2011 includes the $2.0 million one-time pension settlement charge discussed earlier. Excluding the one-time pension charge, net operating expenses not allocated to a business unit increased $1.1 million primarily due to higher professional services fees and other cost inflation.

Non-operating income (expense) as presented in the *Business Unit Performance* table includes $18.7 million of interest expense for 2012 and $31.8 million for 2011. In connection with debt refinancing or redemption initiatives, the reported amounts include $1.9 million and $5.9 million in 2012 and 2011, respectively, related to the write-off of unamortized issuance costs and original issue discount. Excluding these write-offs, interest expense declined to $16.8 million in 2012 compared to $25.9 million in 2011, primarily reflecting the 2011 redemption of $100 million of 7.125% notes.

**Income taxes** In 2012, income tax expense totaled $19.6 million on pre-tax income of $78.9 million. The comparable amounts in 2011 were $8.2 million and $50.8 million, respectively. Tax expense in 2011 includes a net $5.2 million income tax benefit realized in connection with the resolution of certain foreign tax audits, and expiration of statutes of limitation, partially offset by an increase in the valuation allowance on certain net operating loss carryforwards.

In January 2013, the U.S. President signed legislation that retroactively extended the federal research and development tax credit for two years, from January 1, 2012 through December 31, 2013. As a result we expect that our income tax provision for the first quarter of 2013 will include a tax benefit of $1.2 million related to 2012 research and development credits.

**Foreign Currency** We own and operate manufacturing facilities in Canada, Germany, France, the United Kingdom and the Philippines. The functional currency in Canada is the U.S. dollar, in Germany and France the Euro, in the UK it is the British Pound Sterling, and in the Philippines it is the Peso. During 2012, Euro functional currency operations generated approximately 25.3% of net sales and 24.2% of operating expenses and British Pound Sterling operations represented 7.5% of net sales and 7.6% of operating expenses. The translation of the results from international operations into U.S. dollars is subject to changes in foreign currency exchange rates. The table below summarizes the translation impact on reported results that changes in currency exchange rates had on our non-U.S. based operations from the conversion of these operation s results:

| *In thousands* | Year ended December 31, 2012 Favorable (unfavorable) |
|---|---|
| Net sales | **$ (35,818)** |
| Costs of products sold | **26,828** |
| SG&A expenses | **2,813** |
| Income taxes and other | **514** |

| | | |
|---|---|---|
| Net income | **$** | **(5,663)** |

The above table only presents the financial reporting impact of foreign currency translations assuming currency exchange rates in 2012 were the same as 2011. It does not present the impact of certain competitive advantages or disadvantages of operating or competing in multi-currency markets.

***2011 versus 2010***

The following table sets forth summarized consolidated results of operations:

| | Year Ended December 31 | |
|---|---|---|
| *In thousands, except per share* | 2011 | 2010 |
| Net sales | $ 1,603,154 | $ 1,455,331 |
| Gross profit | 206,193 | 186,247 |
| Operating income | 85,272 | 64,589 |
| Net income | 42,694 | 54,434 |
| Earnings per diluted share | 0.93 | 1.17 |

18

Table of Contents

The consolidated results of operations for 2011 and 2010 include the following items not considered to be part of our core business operations:

| *In thousands, except per share* | After-tax Gain (loss) | Diluted EPS |
|---|---|---|
| 2011 | | |
| Early redemption of $100 million bonds | $ (6,065) | $ (0.13) |
| Charge for workforce efficiencies | (652) | (0.01) |
| Acquisition and integration costs | (792) | (0.02) |
| Timberland sales and related transaction costs | 4,160 | 0.09 |
| 2010 | | |
| Cellulosic biofuel/alternative fuel mixture credits | $ 23,184 | $ 0.50 |
| Acquisition and integration costs | (9,073) | (0.20) |
| Foreign currency hedge on acquisition price | (1,673) | (0.04) |
| Timberland sales and related transaction costs | 1,063 | 0.02 |

During 2011, the aggregate effect of the unusual items set forth above decreased earnings by $3.3 million, or $0.07 per diluted share. In 2010, the items set forth above increased earnings by $13.5 million, or $0.28 per diluted share in 2010.

**Business Unit Performance**

| | Year ended December 31 | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| *In millions* | Specialty Papers | | Composite Fibers | | Advanced Airlaid Materials | | Other and Unallocated | | Total | |
| | 2011 | 2010 | 2011 | 2010 | 2011 | 2010 | 2011 | 2010 | 2011 | 2010 |
| Net sales | $ 875.1 | $ 842.6 | $ 476.0 | $ 419.2 | $ 252.0 | $ 193.5 | $ | $ | $ 1,603.2 | $ 1,455.3 |
| Energy and related sales, net | 9.3 | 10.7 | | | | | | | 9.3 | 10.7 |
| Total revenue | 884.4 | 853.3 | 476.0 | 419.2 | 252.0 | 193.5 | | | 1,612.5 | 1,466.0 |
| Cost of products sold | 775.7 | 740.2 | 395.7 | 350.5 | 227.7 | 181.7 | 7.2 | 7.4 | 1,406.3 | 1,279.7 |
| Gross profit | 108.7 | 113.1 | 80.3 | 68.7 | 24.3 | 11.8 | (7.2) | (7.4) | 206.2 | 186.2 |
| SG&A | 51.4 | 54.7 | 39.5 | 35.8 | 10.9 | 7.4 | 23.0 | 24.3 | 124.9 | 122.1 |
| Gains on dispositions of plant, equipment and timberlands | | | | | | | (4.0) | (0.5) | (4.0) | (0.5) |
| Total operating income (loss) | 57.3 | 58.4 | 40.8 | 32.9 | 13.4 | 4.4 | (26.2) | (31.2) | 85.3 | 64.6 |
| Non-operating expense | | | | | | | (34.4) | (31.1) | (34.4) | (31.1) |
| Income (loss) before income taxes | $ 57.3 | $ 58.4 | $ 40.8 | $ 32.9 | $ 13.4 | $ 4.4 | $ (60.7) | $ (62.3) | $ 50.8 | $ 33.5 |
| **Supplementary Data** | | | | | | | | | | |
| Net tons sold *(thousands)* | 779.6 | 764.7 | 93.3 | 90.4 | 88.0 | 72.8 | | | 960.9 | 927.9 |
| Depreciation, depletion and amortization | $ 36.0 | $ 34.9 | $ 24.8 | $ 23.7 | $ 8.5 | $ 7.2 | $ | $ | $ 69.3 | $ 65.8 |
| Capital expenditures | 31.4 | 24.1 | 22.5 | 8.2 | 10.6 | 4.2 | | | 64.5 | 36.5 |

The sum of individual amounts set forth above may not agree to the consolidated financial statements included herein due to rounding.

**Sales and Costs of Products Sold**

| | Year ended December 31 | | |
|---|---|---|---|
| *In thousands* | 2011 | 2010 | Change |
| Net sales | $ 1,603,154 | $ 1,455,331 | $ 147,823 |
| | 9,344 | 10,653 | (1,309) |

| | | | |
|---|---|---|---|
| Energy and related sales net | | | |
| Total revenues | 1,612,498 | 1,465,984 | 146,514 |
| Costs of products sold | 1,406,305 | 1,279,737 | 126,568 |
| Gross profit | $ 206,193 | $ 186,247 | $ 19,946 |
| Gross profit as a percent of Net sales | 12.9% | 12.8% | |

The following table sets forth the contribution to consolidated net sales by each business unit:

| *Percent of Total* | Percent of total 2011 | 2010 |
|---|---|---|
| **Business Unit** | | |
| Specialty Papers | 54.6% | 57.9% |
| Composite Fibers | 29.7 | 28.8 |
| Advanced Airlaid Materials | 15.7 | 13.3 |
| Total | 100.0% | 100.0% |

Table of Contents

Net sales for 2011 were $1,603.2 million, a 10.2% increase compared with $1,455.3 million for 2010, reflecting stronger business activity in the our Composite Fibers and Advanced Airlaid Materials business units together with more favorable selling prices in all businesses. Advanced Airlaid Materials business unit is included for a full year in 2011 compared with only prospectively from the February 12, 2010 acquisition date in the prior year amounts.

In the Specialty Papers business unit, net sales for 2011 increased $32.5 million, or 3.9%, to $875.1 million. The increase was primarily due to a $27.3 million benefit from higher selling prices and a 2.0% increase in volumes shipped.

Specialty Papers operating profit for 2011 declined by $1.1 million compared with 2010 primarily due to pressure on margins as higher input costs of $28.4 million offset benefits of higher selling prices. Net energy revenue declined in the comparison of 2011 to 2010 by $1.3 million.

We sell excess power generated by the Spring Grove, PA facility. In addition, two of our facilities are registered generators of renewable energy credits ( RECs ). The following table summarizes this activity for 2011 and 2010:

| | Year ended December 31 | | |
|---|---|---|---|
| *In thousands* | 2011 | 2010 | Change |
| Energy sales | $ 10,992 | $ 14,296 | $ (3,304) |
| Costs to produce | (9,319) | (10,403) | 1,084 |
| Net | 1,673 | 3,893 | (2,220) |
| Renewable energy credits | 7,671 | 6,760 | 911 |
| Total | $ 9,344 | $ 10,653 | $ (1,309) |

RECs represent sales of certified credits earned related to burning renewable sources of energy such as black liquor and wood waste. We sell RECs into an emerging and somewhat illiquid market. The extent and value of future revenues from REC sales is dependent on many factors outside of management s control. Therefore, we may not be able to generate consistent amounts of sales of RECs in future periods.

In Composite Fibers, net sales for 2011 were $476.0 million, an increase of $56.8 million, or 13.5%, from 2010. The improvement primarily reflects growth in food & beverage market segment, particularly single-serve coffee products. Volumes shipped increased 3.3%, and on a constant currency basis, average selling prices benefitted the comparison by $13.0 million, and the translation of foreign currencies favorably affected net sales by approximately $17.0 million.

Composite Fibers operating profit increased $7.9 million, or 24.0%, in the year over year comparison. The improved performance was driven by higher selling prices as well as improved operating rates, efficiency gains related to continuous improvement initiatives and the impact of an improved mix of products sold. The combination of these factors more than offset the $10.0 million negative impact of higher input costs, primarily related to woodpulp, synthetic fibers and energy. Foreign currency translation unfavorably impacted operating income by $0.5 million.

In Advanced Airlaid Materials, net sales were $252.0 million, an increase of $58.5 million, due to including a full period s results in 2011, higher selling prices and improved demand. The results for 2010 were included prospectively from the February 12, 2010 acquisition date. Higher selling prices benefited the comparison by $12.3 million but were offset by $12.1 million of higher input costs. Operating income increased $9.0 million primarily due to higher volumes shipped, increased selling prices, improved operating efficiencies and a benefit in the comparison of a non-recurring $1.4 million charge in 2010 to cost of products sold for the write up of acquired inventory to fair value. Foreign currency translation unfavorably impacted operating income by $0.4 million.

**Pension Expense** The following table summarizes the amounts of pension expense recognized for 2011 compared to 2010:

| | Year ended December 31 | | |
|---|---|---|---|
| *In thousands* | 2011 | 2010 | Change |
| *Recorded as*: | | | |
| Costs of products sold | $ 6,735 | $ 7,056 | $ (321) |
| SG&A expense | 3,645 | 2,185 | 1,460 |
| Total | $ 10,380 | $ 9,241 | $ 1,139 |

The amount set forth above for pension expense recorded as selling, general and administrative ( SG&A ) expense in 2011 includes a $2.0 million one-time pension settlement charge recorded in connection with the retirement of our former Chief Executive Officer.

The amount of pension expense recognized each year is dependent on various actuarial assumptions and certain other factors, including discount rates and the fair value of our pension assets as of the beginning of the year.

Table of Contents

**Gain on Sales of Plant, Equipment and Timberlands, net** During the years ended December 31, 2011 and 2010, we completed the following sales of assets:

| *Dollars in thousands* | Acres | Proceeds | Gain |
|---|---|---|---|
| 2011 | | | |
| Timberlands | 942 | $ 3,821 | $ 3,590 |
| Other | n/a | 670 | 360 |
| Total | | $ 4,491 | $ 3,950 |
| 2010 | | | |
| Timberlands | 164 | $ 387 | $ 373 |
| Other | n/a | 177 | 80 |
| Total | | $ 564 | $ 453 |

In connection with each of the asset sales set forth above, we received cash proceeds.

**Other and Unallocated** The amount of net operating expenses not allocated to a business unit and reported as Other and Unallocated in our table of *Business Unit Performance,* excluding gains from sales of plant, equipment and timberlands, totaled $30.2 million in 2011 compared with $31.7 million in 2010.

Non-operating income (expense) includes $31.8 million of interest expense for 2011 and $25.5 million for 2010. For 2011, the amount includes $5.9 million related to the write-off of unamortized issuance costs and original issue discount in connection with the early redemption of $100 million of bonds.

Non-operating income (expense) for 2011 also includes a $3.6 million redemption premium incurred in connection with the bond retirement discussed above. In 2010, other non operating expense, net totaled $6.3 million and represented a $3.4 million loss on a series of forward foreign currency contracts to hedge the Concert acquisition s Canadian dollar purchase price. In addition, in connection with purchase accounting for the Concert transaction, we recorded a $2.5 million reserve for tax risks, inclusive of accrued interest, existing at the time of the acquisition and at the same time recorded a $2.5 million receivable from the seller due to an indemnification agreement. During the fourth quarter, a tax ruling was issued that eliminated this tax risk and as a result we recognized an expense of $2.5 million which is presented under the caption Other net in the accompanying consolidated statements of income to eliminate the receivable from the seller. We also recognized a $2.5 million tax benefit for this same item to eliminate the tax reserve previously established resulting in no net impact to earnings during 2010.

**Income taxes** In 2011, income tax expense totaled $8.2 million on pre-tax income of $50.8 million. Tax expense in 2011 includes a net $5.2 million income tax benefit realized in connection with the resolution of certain foreign tax audits, and expiration of statutes of limitation, partially offset by an increase in the valuation allowance on certain net operating loss carryforwards. For 2010, we recorded income tax benefits of $20.9 million on $33.5 million of pretax income. The benefit in 2010 was due to $23.2 million of cellulosic biofuel credits, net, recorded as an income tax benefit in 2010 as discussed further below. We also recorded the $2.5 million tax benefit discussed above, as well as a $6.4 million adjustment to reduce tax liabilities resulting from the expiration of statutes of limitations on uncertain tax positions and other factors.

**Foreign Currency** In 2011, we owned and operated manufacturing facilities in Canada, Germany, France, the United Kingdom and the Philippines. The functional currency in Canada is the U.S. dollar, in Germany and France the Euro, in the UK it is the British Pound Sterling, and in the Philippines it is the Peso. During 2011, Euro functional currency operations generated approximately 28.7% of our sales and 27.2% of operating expenses and British Pound Sterling operations represented 7.6% of net sales and 7.4% of operating expenses. The translation of the results from international operations into U.S. dollars is subject to changes in foreign currency exchange rates. The table below summarizes the translation impact on reported results that changes in currency exchange rates had on our non-U.S. based operations from the conversion of these operation s results:

| *In thousands* | Year Ended December 31, 2011 Favorable (unfavorable) |
|---|---|
| Net sales | $ 23,625 |
| Costs of products sold | (22,380) |
| SG&A expenses | (2,117) |
| Income taxes and other | (352) |

| | | |
|---|---|---|
| Net income | $ | (1,224) |

The above table only presents the financial reporting impact of foreign currency translations assuming currency exchange rates in 2011 were the same as 2010. It does not present the impact of certain competitive advantages or disadvantages of operating or competing in multi-currency markets.

Table of Contents

**LIQUIDITY AND CAPITAL RESOURCES**

Our business is capital intensive and requires significant expenditures for new or enhanced equipment, to support our research and development efforts, for environmental compliance matters including, but not limited to, the Clean Air Act, and to support our business strategy. In addition, we have mandatory debt service requirements of both principal and interest. The following table summarizes cash flow information for each of the years presented:

| | Year ended December 31 | |
|---|---|---|
| *In thousands* | **2012** | 2011 |
| Cash and cash equivalents at beginning of period | **$ 38,277** | $ 95,788 |
| Cash provided (used) by | | |
| Operating activities | **112,846** | 140,307 |
| Investing activities | **(48,705)** | (16,830) |
| Financing activities | **(5,489)** | (180,140) |
| Effect of exchange rate changes on cash | **750** | (848) |
| Net cash provided (used) | **59,402** | (57,511) |
| Cash and cash equivalents at end of period | **$ 97,679** | $ 38,277 |

At the end of the 2012, we had $97.7 million in cash and cash equivalents and $344.8 million available under our revolving credit agreement, which matures in November 2016.

Operating cash flow declined in the year-over-year comparison by $27.5 million primarily due to the use of $6.7 million of cash in 2012, net of credits related to the conversion of alternative fuel mixture credits for cellulosic biofuel production credits. Comparatively, in 2011, we received $17.8 million of cellulosic biofuel credits.

Net cash used by investing activities increased $31.9 million in comparison of 2012 to 2011, largely due to the $43.2 million cash received in 2011 from proceeds under a timberland installment note receivable. Capital expenditures totaled $58.8 million in 2012 compared with $64.5 million in 2011 and are expected to approximate $90 million to $100 million in 2013, including $33.5 million to complete the $50 million investment to expand capacity to serve Composite Fibers growth markets.

Net cash used by financing activities totaled $5.5 million in 2012 and $180.1 million in 2011, primarily reflecting the net effects of debt repayments or refinancing and common share repurchases. In 2012, as discussed below, we issued $250.0 million of 5.375% bonds and used the proceeds to repay all amounts outstanding under our revolving credit agreement and to redeem $200.0 million of 7.125% notes together with a redemption premium and consent fee of $5.1 million. In 2011, we

redeemed $100.0 million of 7.125% bonds and paid an early redemption premium of $3.6 million, and repaid a $36.7 million term loan in connection with the collection of the installment note discussed above.

The following table sets forth our outstanding long-term indebtedness:

| | December 31 | |
|---|---|---|
| *In thousands* | **2012** | 2011 |
| Revolving credit facility, due Nov. 2016 | **$** | $ 27,000 |
| 5.375% Notes, due Nov 2020 | **250,000** | |
| 7.125% Notes, due May 2016 | | 200,000 |
| Total long-term debt | **250,000** | 227,000 |
| Less current portion | | |
| Long-term debt, net of current portion | **$ 250,000** | $ 227,000 |

Our revolving credit facility contains a number of customary compliance covenants. In addition, the 5.375% Notes contain cross default provisions that could result in all such notes becoming due and payable in the event of a failure to repay debt outstanding under the credit agreement at maturity, or a default under the credit agreement, that accelerates the debt outstanding thereunder. As of December 31, 2012, we met all of the requirements of our debt covenants. The significant terms of the debt instruments are more fully discussed in Item 8 Financial Statements Note 15.

On October 3, 2012, we completed an offering of $250.0 million aggregate principal amount of 5.375% Senior Notes due 2020. The net proceeds from this offering totaled approximately $245.1 million, after deducting the commissions and other fees and expenses relating to the offering.

Cash used for common share repurchases totaled $5.7 million in 2012, and $48.0 million in 2011. The amount for 2012 includes $1.2 million under a $50 million program authorized in 2011. In May 2012, our Board of Directors authorized a second share repurchase program for up to $25.0 million, exclusive of commissions, of our outstanding common stock. The following table summarizes share repurchases made under this program through December 31, 2012:

| | shares | *(thousands)* |
|---|---|---|
| Authorized amount | n/a | $ 25,000 |
| Repurchases | 291,120 | (4,462) |
| Remaining authorization | | $ 20,538 |

During 2012 and 2011, cash dividends paid on common stock totaled $15.6 million and $16.6 million, respectively. The decline was due to the impact of our share repurchase programs. Our Board of Directors

22

determines what, if any, dividends will be paid to our shareholders. Dividend payment decisions are based upon then-existing factors and conditions and, therefore, historical trends of dividend payments are not necessarily indicative of future payments.

We are subject to various federal, state and local laws and regulations intended to protect the environment as well as human health and safety. At various times, we have incurred significant costs to comply with these regulations and we could incur additional costs as new regulations are developed or regulatory priorities change. As a result of new air quality regulations including the U.S. EPA Best Available Retrofit Technology rule (BART; otherwise known as the Regional Haze Rule) and the Boiler Maximum Achievable Control Technology rule (Boiler MACT), we anticipate that we could incur material capital and operating costs. For example, on December 20, 2012, the Administrator of the U. S. Environmental Protection Agency signed new rules which could require process modifications and/or installation of air pollution controls on power boilers at two of our facilities. We are currently reviewing these rules to understand the effect they may have on our operations, such as reducing or curtailing boiler usage or modifying the types of boilers operated or fuel consumed. The cost of compliance is likely to be significant. Our current estimates to implement viable options could result in additional capital spending of approximately $45 million. The amount ultimately incurred may be less depending on our successful implementation

of appropriate available options. In addition, the timing of any additional capital spending is uncertain, although we currently expect to incur the expenditures generally in 2015 and 2016. Enactment of new environmental laws or regulations or changes in existing laws or regulations could significantly change our estimates.

In addition, we may incur obligations to remove or mitigate any adverse effects on the environment resulting from our operations, including the restoration of natural resources and liability for personal injury and for damages to property and natural resources. See Item 8 Financial Statements and Supplementary Data Note 21 for a summary of significant environmental matters.

We expect to meet all of our near and long-term cash needs from a combination of operating cash flow, cash and cash equivalents, and our existing credit facilities. However, an unfavorable outcome of various environmental matters could have a material adverse impact on our consolidated financial position, liquidity and/or results of operations.

**Off-Balance-Sheet Arrangements** As of December 31, 2012 and 2011, we had not entered into any off-balance-sheet arrangements. Financial derivative instruments to which we are a party and guarantees of indebtedness, which solely consist of obligations of subsidiaries and a partnership, are reflected in the condensed consolidated balance sheets included herein in Item 8 Financial Statements and Supplementary Data.

**Contractual Obligations** The following table sets forth contractual obligations as of December 31, 2012:

| | | Payments Due During the Year Ended December 31, | | | |
|---|---|---|---|---|---|
| *In millions* | Total | 2013 | 2014 to 2015 | 2016 to 2017 | 2018 and beyond |
| Long-term debt[(1)] | $ 357 | $ 13 | $ 27 | $ 27 | $ 290 |
| Operating leases[(2)] | 21 | 5 | 6 | 4 | 6 |
| Purchase obligations[(3)] | 204 | 134 | 68 | 2 | 0 |
| Other long term obligations[(4),(5)] | 76 | 9 | 17 | 14 | 36 |
| Total | $ 658 | $ 161 | $ 118 | $ 47 | $ 332 |

(1) Represents principal and interest payments due on long-term debt, the significant terms of which are discussed in Item 8 Financial Statements, Note 15, Long-term Debt.

(2) Represents rental agreements for various land, buildings, vehicles, and computer and office equipment.

(3) Represents open purchase order commitments and other obligations, primarily for raw material forward purchases and pulpwood contracts with minimum annual purchase obligations. In certain situations, prices are subject to variations based on market prices. In such situations, the information above is based on prices in effect at December 31, 2012 or expectations based on historical experience and/or current market conditions.

(4) Primarily represents expected benefits to be paid pursuant to retirement medical plans and nonqualified pension plans over the next ten years and expected costs of asset retirement obligations.

(5) Since we are unable to reasonably estimate the timing of ultimate payment, the amounts set forth above do not include any payments that may be made related to uncertain tax positions, including potential interest, accounted for in accordance with ASC 740-10-20. As discussed in more detail in Item 8 Financial Statements, Note 7, Income Taxes , such amounts totaled $30.4 million at December 31, 2012.

Table of Contents

**Critical Accounting Policies and Estimates** The preceding discussion and analysis of our consolidated financial position and results of operations is based upon our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these consolidated financial statements requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosures of contingent assets and liabilities. On an on-going basis, we evaluate our estimates, including those related to inventories, long-lived assets, pension and post-retirement obligations, environmental liabilities and income taxes. We base our estimates on historical experience and on various other assumptions that we believe are reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

We believe the following represent the most significant and subjective estimates used in the preparation of our consolidated financial statements.

**Long-lived Assets** We evaluate the recoverability of our long-lived assets, including plant, equipment, timberlands, goodwill and other intangible assets periodically or whenever events or changes in circumstances indicate that the carrying amounts may not be recoverable. Our evaluations include considerations of a variety of qualitative factors and, if warranted, analyses based on the cash flows generated by the underlying assets, profitability information, including estimated future operating results, trends or other determinants of fair value. If the value of an asset determined by these evaluations is less than its carrying amount, a loss is recognized for the difference between the fair value and the carrying value of the asset. Future adverse changes in market conditions or poor operating results of the related business may indicate an inability to recover the carrying value of the assets, thereby possibly requiring an impairment charge in the future.

**Pension and Other Post-Retirement Obligations** Accounting for defined-benefit pension plans, and any curtailments thereof, requires various assumptions, including, but not limited to, discount rates, expected long-term rates of return on plan assets and future compensation growth rates. Accounting for our retiree medical plans, and any curtailments thereof, also requires various assumptions, which include, but are not limited to, discount rates and annual rates of increase in the per capita costs of health care benefits.

The following chart summarizes the more significant assumption used in the actuarial valuation of our defined-benefit plans for each of the past three years:

| | **2012** | 2011 | 2010 |
|---|---|---|---|
| **Pension plans** | | | |
| Weighted average discount rate | **4.28%** | 5.09% | 5.80% |
| Expected long-term rate of return on plan assets | **8.50** | 8.50 | 8.50 |
| Rate of compensation increase | **4.00** | 4.00 | 4.00 |
| **Post-retirement medical** | | | |
| Weighted average discount rate | **3.58** | 4.45 | 5.10 |
| Health care cost trend rate assumed for next year | **7.68** | 7.90 | 8.10 |
| Ultimate cost trend rate | **4.50** | 4.50 | 4.50 |
| Year that the ultimate cost trend rate is reached | **2028** | 2028 | 2021 |

We evaluate these assumptions at least once each year or as facts and circumstances dictate and we make changes as conditions warrant. Changes to these assumptions will increase or decrease our reported net periodic benefit expense, which will result in changes to the recorded benefit plan assets and liabilities.

**Environmental Liabilities** We maintain accruals for losses associated with environmental obligations when it is probable that a liability has been incurred and the amount of the liability can be reasonably estimated based on existing legislation and remediation technologies. These accruals are adjusted periodically as assessment and remediation actions continue and/or further legal or technical information develops. Such undiscounted liabilities are exclusive of any insurance or other claims against third parties. Recoveries of environmental remediation costs from other parties, including insurance carriers, are recorded as assets when their receipt is assured beyond a reasonable doubt.

**Income Taxes** We record the estimated future tax effects of temporary differences between the tax bases of assets and liabilities and amounts reported in our balance sheets, as well as operating loss and tax credit carry forwards. These deferred tax assets and liabilities are measured using enacted tax rates and laws that will be in effect when such amounts are expected to reverse or be utilized. We regularly review our deferred tax assets for recoverability based on historical taxable income, projected future taxable income, the expected timing of the reversals of existing temporary differences and tax planning strategies. If we are unable to generate sufficient future taxable income, or if there is a material change in the actual effective tax rates or time period within which the underlying temporary differences become taxable or deductible, we could be required to increase the valuation

24

Table of Contents

allowance against our deferred tax assets, which may result in a substantial increase in our effective tax rate and a material adverse impact on our reported results.

Significant judgment is required in determining our worldwide provision for income taxes and recording the related assets and liabilities. In the ordinary course of our business, there are many transactions and calculations where the ultimate tax determination is less than certain. We and our subsidiaries are examined by various Federal, State and foreign tax authorities. We regularly assess the potential outcomes of these examinations and any future examinations for the current or prior years in determining

the adequacy of our provision for income taxes. We continually assess the likelihood and amount of potential adjustments and adjust the income tax provision, the current liability and deferred taxes in the period in which the facts that give rise to a revision become known.

Other significant accounting policies, not involving the same level of uncertainties as those discussed above, are nevertheless important to an understanding of the Consolidated Financial Statements. Refer to Item 8 Financial Statements and Supplementary Data Notes to Consolidated Financial Statements for additional accounting policies.

## *ITEM 7A QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK*

| | Year Ended December 31 | | | | | At December 31, 2012 | |
|---|---|---|---|---|---|---|---|
| *Dollars in thousands* | 2013 | 2014 | 2015 | 2016 | 2017 | Carrying Value | Fair Value |
| **Long-term debt** | | | | | | | |
| Average principal outstanding | | | | | | | |
| At fixed interest rates Bond | $ 250,000 | $ 250,000 | $ 250,000 | $ 250,000 | $ 250,000 | $ 250,000 | $ 260,340 |
| At variable interest rates | | | | | | | |
| | | | | | | $ 250,000 | $ 260,340 |
| Weighted-average interest rate | | | | | | | |
| On fixed rate debt Bond | 5.375% | 5.375% | 5.375% | 5.375% | 5.375% | | |
| On variable rate debt | | | | | | | |

The table above presents the average principal outstanding and related interest rates for the next five years for debt outstanding as of December 31, 2012. Fair values included herein have been determined based upon rates currently available to us for debt with similar terms and remaining maturities.

Our market risk exposure primarily results from changes in interest rates and currency exchange rates. At December 31, 2012, we had long-term debt outstanding of $250.0 million, all of which was at fixed rates.

As part of our overall risk management practices, we enter into financial derivatives primarily designed to either i) hedge foreign currency risks associated with forecasted transactions cash flow hedges ; or ii) mitigate the

impact that changes in currency exchange rates have on intercompany financing transactions and foreign currency denominated receivables and payables foreign currency hedges. For a more complete discussion of this activity, refer to Item 8 Financial Statements and Supplementary Data Note 18.

We are subject to certain risks associated with changes in foreign currency exchange rates to the extent our operations are conducted in currencies other than the U.S. dollar. During 2012, Euro functional currency operations generated approximately 25.3% of net sales and 24.2% of operating expenses and British Pound Sterling operations represented 7.5% of net sales and 7.6% of operating expenses.

Table of Contents

*ITEM 8 FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA*
**MANAGEMENT S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING**

Management of P. H. Glatfelter Company (the Company ) is responsible for establishing and maintaining adequate internal control over financial reporting. The Company s internal control over financial reporting is a process designed under the supervision of the chief executive and chief financial officers to provide reasonable assurance regarding the reliability of financial reporting and the preparation of the Company s financial statements for external reporting purposes in accordance with accounting principles generally accepted in the United States.

As of December 31, 2012, management conducted an assessment of the effectiveness of the Company s internal control over financial reporting based on the framework established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Management has determined that the Company s internal control over financial reporting as of December 31, 2012, is effective to provide reasonable assurance regarding the reliability of financial reporting and the preparation of the Company s financial statements for external reporting purposes in accordance with accounting principles generally accepted in the United States.

The Company s internal control over financial reporting includes policies and procedures that pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect transactions and dispositions of assets; provide reasonable assurances that transactions are recorded as necessary to permit preparation of financial statements in accordance with accounting principles generally accepted in the United States, and that receipts and expenditures are being made only in accordance with authorizations of management; and provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Company s assets that could have a material effect on our financial statements.

The Company s internal control over financial reporting as of December 31, 2012, has been audited by Deloitte & Touche LLP, an independent registered public accounting firm, as stated in their reports appearing herein, which expresses an unqualified opinion on the effectiveness of the Company s internal control over financial reporting as of December 31, 2012.

The Company s management, including the chief executive officer and chief financial officer, does not expect that our internal control over financial reporting will prevent or detect all errors and all frauds. A control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the control system s objectives will be met. The design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Further, because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that misstatements due to error or fraud will not occur or that all control issues and instances of fraud, if any, within the Company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty and that breakdowns can occur because of simple error or mistake. Controls can also be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the controls. The design of any system of controls is based, in part, on certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Projections of any evaluation of controls effectiveness to future periods are subject to risks. Over time, controls may become inadequate because of changes in conditions or deterioration in the degree of compliance with policies or procedures.

**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

To the Board of Directors and Shareholders of P. H. Glatfelter Company

We have audited the internal control over financial reporting of P.H. Glatfelter Company and subsidiaries (the Company ) as December 31, 2012, based on the criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Company s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management s Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on the Company s internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company s internal control over financial reporting is a process designed by, or under the supervision of, the company s principal executive and principal financial officers, or persons performing similar functions, and effected by the company s board of directors, management, and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company s internal control over financial reporting includes those policies and procedures that

(1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company s assets that could have a material effect on the financial statements.

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2012, based on the criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated financial statements and financial statement schedule as of and for the year ended December 31, 2012 of the Company and our report dated March 7, 2013 expressed an unqualified opinion on those financial statements and financial statement schedule.

/s/ DELOITTE & TOUCHE LLP

Philadelphia, Pennsylvania

March 7, 2013

Table of Contents

**REPORT OF INDEPENDENT REGISTERED PUBLIC**

**ACCOUNTING FIRM**

To the Board of Directors and Shareholders of P. H. Glatfelter Company

We have audited the accompanying consolidated balance sheets of P.H. Glatfelter Company and subsidiaries (the Company ) as of December 31, 2012 and 2011, and the related consolidated statements of income, comprehensive income, shareholders equity, and cash flows for each of the three years in the period ended December 31, 2012. Our audits also included the financial statement schedule listed in the Index at Item 15. These financial statements and financial statement schedule are the responsibility of the Company s management. Our responsibility is to express an opinion on the financial statements and financial statement schedule based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of P. H. Glatfelter Company and subsidiaries as of December 31, 2012 and 2011, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2012, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, such financial statement schedules, when considered in relation to the basic consolidated financial statements taken as a whole, present fairly, in all material respects, the information set forth therein.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company s internal control over financial reporting as of December 31, 2012, based on the criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated March 7, 2013 expressed an unqualified opinion on the Company s internal control over financial reporting.

/s/ DELOITTE & TOUCHE LLP

Philadelphia, Pennsylvania

March 7, 2013

Table of Contents

**P. H. GLATFELTER COMPANY and SUBSIDIARIES**

**CONSOLIDATED STATEMENTS OF INCOME**

| *In thousands, except per share* | Year ended December 31<br>**2012** | <br>2011 | <br>2010 |
|---|---|---|---|
| Net sales | **$ 1,577,788** | $ 1,603,154 | $ 1,455,331 |
| Energy and related sales, net | **7,000** | 9,344 | 10,653 |
| Total revenues | **1,584,788** | 1,612,498 | 1,465,984 |
| Costs of products sold | **1,371,139** | 1,406,305 | 1,279,737 |
| Gross profit | **213,649** | 206,193 | 186,247 |
| Selling, general and administrative expenses | **121,590** | 124,871 | 122,111 |
| Gains on dispositions of plant, equipment and timberlands, net | **(9,815)** | (3,950) | (453) |
| Operating income | **101,874** | 85,272 | 64,589 |
| Non-operating income (expense) | | | |
| Interest expense | **(18,694)** | (31,794) | (25,547) |
| Interest income | **460** | 666 | 808 |
| Other, net | **(4,699)** | (3,299) | (6,321) |
| Total other income (expense) | **(22,933)** | (34,427) | (31,060) |
| Income before income taxes | **78,941** | 50,845 | 33,529 |
| Income tax provision (benefit) | **19,562** | 8,151 | (20,905) |
| Net income | **$ 59,379** | $ 42,694 | $ 54,434 |
| | | | |
| **Earnings per share** | | | |
| Basic | **$ 1.39** | $ 0.94 | $ 1.19 |
| Diluted | **1.36** | 0.93 | 1.17 |
| | | | |
| **Weighted average shares outstanding** | | | |
| Basic | **42,851** | 45,228 | 45,922 |
| Diluted | **43,672** | 45,794 | 46,374 |

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

Table of Contents

**P. H. GLATFELTER COMPANY AND SUBSIDIARIES**

**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**

| | Year ended December 31 | | |
|---|---|---|---|
| *In thousands* | **2012** | 2011 | 2010 |
| Net income | **$ 59,379** | $ 42,694 | $ 54,434 |
| Foreign currency translation adjustments | **11,358** | (10,160) | (17,227) |
| Net change in: | | | |
| Deferred gains (losses) on cash flow hedges, net of taxes of $638, $(464) and $0, respectively | **(1,609)** | 1,185 | |
| Unrecognized retirement obligations, net of taxes of $3,914, $22,672, and $(9,905), respectively | **(6,974)** | (36,519) | 15,865 |
| Other comprehensive income (loss) | **2,775** | (45,494) | (1,362) |
| Comprehensive income (loss) | **$ 62,154** | $ (2,800) | $ 53,072 |

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

30

Table of Contents

**P. H. GLATFELTER COMPANY and SUBSIDIARIES**

**CONSOLIDATED BALANCE SHEETS**

| *In thousands* | December 31 2012 | 2011 |
|---|---|---|
| **Assets** | | |
| Cash and cash equivalents | **$ 97,679** | $ 38,277 |
| Accounts receivable (less allowance for doubtful accounts: 2012 $2,858; 2011 $2,861) | **139,904** | 135,412 |
| Inventories | **222,366** | 206,707 |
| Prepaid expenses and other current assets | **58,909** | 42,017 |
| Total current assets | **518,858** | 422,413 |
| Plant, equipment and timberlands, net | **621,186** | 601,950 |
| Other assets | **102,941** | 112,562 |
| Total assets | **$ 1,242,985** | $ 1,136,925 |
| **Liabilities and Shareholders Equity** | | |
| Accounts payable | **$ 133,389** | $ 109,490 |
| Dividends payable | **3,905** | 3,902 |
| Environmental liabilities | **125** | 250 |
| Other current liabilities | **113,489** | 97,598 |
| Total current liabilities | **250,908** | 211,240 |
| Long-term debt | **250,000** | 227,000 |
| Deferred income taxes | **62,046** | 69,791 |
| Other long-term liabilities | **140,352** | 138,490 |
| Total liabilities | **703,306** | 646,521 |
| Commitments and contingencies | | |
| **Shareholders equity** | | |
| Common stock, $0.01 par value; authorized 120,000,000 shares; issued 54,361,980 shares (including shares in treasury: 2012 11,578,028; 2011 11,711,536) | **544** | 544 |
| Capital in excess of par value | **52,492** | 51,477 |
| Retained earnings | **819,593** | 775,825 |
| Accumulated other comprehensive loss | **(163,966)** | (166,741) |
| | **708,663** | 661,105 |
| Less cost of common stock in treasury | **(168,984)** | (170,701) |
| Total shareholders equity | **539,679** | 490,404 |
| Total liabilities and shareholders equity | **$ 1,242,985** | $ 1,136,925 |

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

Table of Contents

**P.H. GLATFELTER COMPANY and SUBSIDIARIES**

**CONSOLIDATED STATEMENTS OF CASH FLOWS**

| | Year ended December 31 | | |
|---|---|---|---|
| *In thousands* | **2012** | 2011 | 2010 |
| **Operating activities** | | | |
| Net income | **$ 59,379** | $ 42,694 | $ 54,434 |
| Adjustments to reconcile to net cash provided by operations: | | | |
| Depreciation, depletion and amortization | **69,500** | 69,313 | 65,839 |
| Amortization of debt issue costs and original issue discount | **3,177** | 8,838 | 2,758 |
| Pension expense, net of unfunded benefits paid | **10,427** | 2,127 | 8,637 |
| Deferred income tax provision (benefit) | **(2,209)** | 333 | (16,815) |
| Gains on dispositions of plant, equipment and timberlands, net | **(9,815)** | (3,950) | (453) |
| Share-based compensation | **6,520** | 5,762 | 5,767 |
| Change in operating assets and liabilities | | | |
| Accounts receivable | **(3,379)** | 3,771 | (598) |
| Inventories | **(12,615)** | (7,280) | (7,592) |
| Prepaid and other current assets | **(14,952)** | 2,115 | (13,318) |
| Accounts payable | **6,953** | 13,606 | 21,064 |
| Environmental matters | **(151)** | (57) | (29) |
| Accruals and other current liabilities | **15,134** | (2,516) | (1,490) |
| Cellulosic biofuel and alternative fuel mixture credits | **(6,728)** | 17,833 | 54,880 |
| Other | **(8,395)** | (12,282) | (5,079) |
| Net cash provided by operating activities | **112,846** | 140,307 | 168,005 |
| **Investing activities** | | | |
| Expenditures for purchases of plant, equipment and timberlands | **(58,752)** | (64,491) | (36,491) |
| Proceeds from disposals of plant, equipment and timberlands, net | **10,272** | 4,491 | 564 |
| Proceeds from timberland installment sale note receivable | | 43,170 | |
| Acquisitions, net of cash acquired | | | (228,290) |
| Other | **(225)** | | |
| Net cash used by investing activities | **(48,705)** | (16,830) | (264,217) |
| **Financing activities** | | | |
| Proceeds from note offerings | **250,000** | | 95,000 |
| Repayments of note offerings | **(205,131)** | (103,563) | |
| Net borrowings under (repayments of) revolving credit facility | **(27,000)** | 27,000 | |
| Payments of note offering costs | **(4,748)** | (1,672) | (5,340) |
| Repayment of term loans | | (36,695) | (14,000) |
| Net repayments of other short term debt | | (798) | (3,208) |
| Repurchases of common stock | **(5,675)** | (48,033) | |
| Payments of dividends | **(15,608)** | (16,611) | (16,746) |
| Proceeds from stock options exercised and other | **2,673** | 232 | 3,975 |
| Net cash (used) provided by financing activities | **(5,489)** | (180,140) | 59,681 |
| Effect of exchange rate changes on cash | **750** | (848) | (3,101) |
| Net increase (decrease) in cash and cash equivalents | **59,402** | (57,511) | (39,632) |
| Cash and cash equivalents at the beginning of period | **38,277** | 95,788 | 135,420 |
| Cash and cash equivalents at the end of period | **$ 97,679** | $ 38,277 | $ 95,788 |
| | | | |
| **Supplemental cash flow information** | | | |
| Cash paid (received) for: | | | |
| Interest, net of amounts capitalized | **$ 14,400** | $ 24,191 | $ 23,193 |
| Income taxes, net | **44,657** | (8,344) | (40,265) |

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

32

Table of Contents

**P. H. GLATFELTER COMPANY and SUBSIDIARIES**

**CONSOLIDATED STATEMENTS OF SHAREHOLDERS EQUITY**

**For the Years Ended December 31, 2012, 2011 and 2010**

| *In thousands* | Common Stock | Capital in Excess of Par Value | Retained Earnings | Accumulated Other Comprehensive Loss | Treasury Stock | Total Shareholders Equity |
|---|---|---|---|---|---|---|
| Balance at January 1, 2010 | $ 544 | $ 46,746 | $ 711,765 | $ (119,885) | $ (128,466) | $ 510,704 |
| Net income | | | 54,434 | | | 54,434 |
| Other comprehensive loss | | | | (1,362) | | (1,362) |
| Comprehensive income | | | | | | 53,072 |
| Tax effect on employee stock options exercised | | (50) | | | | (50) |
| Cash dividends declared ($0.36 per share) | | | (16,746) | | | (16,746) |
| Share-based compensation expense | | 3,962 | | | | 3,962 |
| Delivery of treasury shares | | | | | | |
| RSUs | | (2,152) | | | 1,662 | (490) |
| 401 (k) plans | | (318) | | | 1,960 | 1,642 |
| Director compensation | | (16) | | | 179 | 163 |
| Employee stock options exercised net | | (27) | | | 212 | 185 |
| Balance at December 31, 2010 | 544 | 48,145 | 749,453 | (121,247) | (124,453) | 552,442 |
| Net income | | | 42,694 | | | 42,694 |
| Other comprehensive income | | | | (45,494) | | (45,494) |
| Comprehensive loss | | | | | | (2,800) |
| Tax effect on employee stock options exercised | | 90 | | | | 90 |
| Cash dividends declared ($0.36 per share) | | | (16,322) | | | (16,322) |
| Share-based compensation expense | | 3,633 | | | | 3,633 |
| Repurchase of common shares | | | | | (48,904) | (48,904) |
| Delivery of treasury shares | | | | | | |
| RSUs | | (215) | | | 215 | |
| 401 (k) plans | | (141) | | | 2,108 | 1,967 |
| Director compensation | | (13) | | | 177 | 164 |
| Employee stock options exercised net | | (22) | | | 156 | 134 |
| Balance at December 31, 2011 | 544 | 51,477 | 775,825 | (166,741) | (170,701) | 490,404 |
| Net income | | | **59,379** | | | **59,379** |
| Other comprehensive income | | | | **2,775** | | **2,775** |
| Comprehensive income | | | | | | **62,154** |
| Tax effect on employee stock options exercised | | **631** | | | | **631** |
| Cash dividends declared ($0.36 per share) | | | **(15,611)** | | | **(15,611)** |
| Share-based compensation expense | | **3,970** | | | | **3,970** |
| Repurchase of common shares | | | | | **(5,675)** | **(5,675)** |
| Delivery of treasury shares | | | | | | |
| RSUs | | **(1,433)** | | | **1,096** | **(337)** |
| 401 (k) plans | | **234** | | | **2,212** | **2,446** |
| Employee stock options exercised net | | **(2,387)** | | | **4,084** | **1,697** |

| | | | | | | |
|---|---|---|---|---|---|---|
| Balance at December 31, 2012 | **$ 544** | **$ 52,492** | **$ 819,593** | **$ (163,966)** | **$ (168,984)** | **$ 539,679** |

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

Table of Contents

**P. H. GLATFELTER COMPANY**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**1. ORGANIZATION**

P. H. Glatfelter Company and subsidiaries ( Glatfelter ) is a manufacturer of specialty papers and fiber-based engineered materials. Headquartered in York, Pennsylvania, our manufacturing facilities are located in Spring Grove, Pennsylvania; Chillicothe and Freemont, Ohio; Gatineau, Quebec, Canada; Lydney, England; Caerphilly, Wales; Gernsbach and Falkenhagen, Germany; Scaër, France; and the Philippines. Our products are marketed worldwide, either through wholesale paper merchants, brokers and agents, or directly to customers.

**2. ACCOUNTING POLICIES**

**Principles of Consolidation** The consolidated financial statements include the accounts of Glatfelter and its wholly owned subsidiaries. All intercompany balances and transactions have been eliminated.

**Accounting Estimates** The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingencies as of the balance sheet date and the reported amounts of revenues and expenses during the reporting period. Management believes the estimates and assumptions used in the preparation of these consolidated financial statements are reasonable, based upon currently available facts and known circumstances, but recognizes that actual results may differ from those estimates and assumptions.

**Cash and Cash Equivalents** We classify all highly liquid instruments with an original maturity of three months or less at the time of purchase as cash equivalents.

**Inventories** Inventories are stated at the lower of cost or market. Raw materials, in-process and finished inventories of our U.S. manufacturing operations are valued using the last-in, first-out (LIFO) method, and the supplies inventories are valued principally using the average-cost method. Inventories at our foreign operations are valued using the average cost method.

**Plant, Equipment and Timberlands** For financial reporting purposes, depreciation is computed using the straight-line method over the estimated useful lives of the respective assets.

The range of estimated service lives used to calculate financial reporting depreciation for principal items of plant and equipment are as follows:

| | | |
|---|---|---|
| Buildings | 10 | 45 Years |
| Machinery and equipment | 7 | 35 Years |
| Other | 4 | 40 Years |

**Maintenance and Repairs** Maintenance and repairs costs are charged to income and major renewals and betterments are capitalized. At the time property is retired or sold, the net carrying value is eliminated and any resultant gain or loss is included in income.

**Valuation of Long-lived Assets, Intangible Assets and Goodwill** We evaluate long-lived assets for impairment when a specific event indicates that the carrying value of an asset may not be recoverable. Recoverability is assessed based on estimates of future cash flows expected to result from the use and eventual disposition of the asset. If the sum of expected undiscounted cash flows is less than the carrying value of the asset, the asset s fair value is estimated and an impairment loss is recognized for any deficiencies. Goodwill is reviewed, on a discounted cash flow basis, during the third quarter of each year for impairment or more frequently if impairment indicators are present. Impairment losses, if any, are recognized for the amount by which the carrying value of the reporting unit exceeds its fair value. The carrying value of a reporting unit is defined using an enterprise premise which is generally determined by the difference between the unit s assets and operating liabilities.

**Asset Retirement Obligations** In accordance with the Financial Accounting Standards Board ( FASB ) Accounting Standards Codification ( ASC ) No. 410, *Asset Retirement and Environmental Obligations,* we accrue asset retirement obligations in the period in which obligations relating to future asset retirements are incurred and when a reasonable estimate of fair value can be determined. Under these standards, costs are to be accrued at estimated fair value, and a related long-lived asset is capitalized. Over time, the liability is accreted to its settlement value and the capitalized cost is depreciated over the useful life of the related asset for which the obligation exists. Upon settlement of the liability, we recognize a gain or loss for any difference between the settlement amount and the liability recorded.

Table of Contents

**Income Taxes** Income taxes are determined using the asset and liability method of accounting for income taxes in accordance with FASB ASC 740 *Income Taxes* ( ASC 740 ). Under ASC 740, tax expense includes U.S. and international income taxes plus the provision for U.S. taxes on undistributed earnings of international subsidiaries not deemed to be permanently invested. Tax credits and other incentives reduce tax expense in the year the credits are claimed. Certain items of income and expense are not reported in tax returns and financial statements in the same year. The tax effect of such temporary differences is reported in deferred income taxes. Deferred tax assets are recognized if it is more likely than not that the assets will be realized in future years. We establish a valuation allowance for deferred tax assets for which realization is not more likely than not.

Income tax contingencies are accounted for in accordance with FASB ASC 740-10-20 *Income Taxes*. Significant judgment is required in determining our worldwide provision for income taxes and recording the related assets and liabilities. In the ordinary course of our business, there are many transactions and calculations where the ultimate tax determination is less than certain. We and our subsidiaries are examined by various Federal, State, and foreign tax authorities. We regularly assess the potential outcomes of these examinations and any future examinations for the current or prior years in determining the adequacy of our provision for income taxes. We continually assess the likelihood and amount of potential adjustments and record any necessary adjustments in the period in which the facts that give rise to a revision become known.

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

**Foreign Currency Translation** Foreign currency translation gains and losses and the effect of exchange rate changes on transactions designated as hedges of net foreign investments are included as a component of other comprehensive income (loss). Transaction gains and losses are included in income in the period in which they occur.

**Revenue Recognition** We recognize revenue on product sales when the customer takes title and assumes the risks and rewards of ownership. Estimated costs for sales incentives, discounts and sales returns and allowances are recorded as sales deductions in the period in which the related revenue is recognized.

Revenue from energy sales is recognized when electricity is delivered to the customer. Certain costs

associated with the production of electricity, such as fuel, labor, depreciation and maintenance are netted against energy sales for presentation on the Consolidated Statements of Income. Our fixed-price contract to sell electricity generated in excess of our own use expired March 31, 2010. Subsequent to the expiration, we now sell excess power at market-rates.

Revenue from renewable energy credits is recorded under the caption Energy and related sales in the Consolidated Statements of Income and is recognized when all risks, rights and rewards to the certificate are transferred to the counterparty.

**Environmental Liabilities** Accruals for losses associated with environmental obligations are recorded when it is probable that a liability has been incurred and the amount of the liability can be reasonably estimated based on existing legislation and remediation technologies. Costs related to environmental remediation are charged to expense. These accruals are adjusted periodically as assessment and remediation actions continue and/or further legal or technical information develops. Such undiscounted liabilities are exclusive of any insurance or other claims against third parties. Environmental costs are capitalized if the costs extend the life of the asset, increase its capacity and/or mitigate or prevent contamination from future operations. Recoveries of environmental remediation costs from other parties, including insurance carriers, are recorded as assets when their receipt is assured beyond a reasonable doubt.

**Earnings Per Share** Basic earnings per share is computed by dividing net income by the weighted-average common shares outstanding during the respective periods. Diluted earnings per share is computed by dividing net income by the weighted-average common shares and common share equivalents outstanding during the period. The dilutive effect of common share equivalents is considered in the diluted earnings per share computation using the treasury stock method.

**Financial Derivatives and Hedging Activities** We use financial derivatives to manage exposure to changes in foreign currencies. In accordance with FASB *ASC 815 Derivatives and Hedging* ( ASC 815 ), we record all derivatives on the balance sheet at fair value. The accounting for changes in the fair value of derivatives depends on the intended use of the derivative, whether we have elected to designate a derivative in a hedging relationship and apply hedge accounting, and whether the hedging relationship has satisfied the criteria necessary to apply hedge accounting.

**Table of Contents**

*Cash Flow Hedges*  The effective portion of the gain or loss on those derivative instruments designated and qualifying as a hedge of the exposure to variability in expected future cash flows related to forecasted transactions is deferred and reported as a component of accumulated other comprehensive income (loss). Deferred gains or losses are reclassified to our results of operations at the time the hedged forecasted transaction is recorded in our results of operations. The effectiveness of cash flow hedges is assessed at inception and quarterly thereafter. If the instrument becomes ineffective or it becomes probable that the originally  forecasted transaction will not occur, the related change in fair value of the derivative instrument is also reclassified from accumulated other comprehensive income (loss) and recognized in earnings.

**Fair Value of Financial Instruments**  Under the accounting for fair value measurements and disclosures, a fair value hierarchy was established that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). A financial instrument s level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. The three levels of the fair value hierarchy are described below:

| | |
|---|---|
| Level 1 | Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities. |
| Level 2 | Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly, including<br>quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar assets or liabilities in markets that are not active; inputs other than quoted prices that are observable for the asset or liability (e.g., interest rates); and inputs that are derived principally from or corroborated by observable market data by correlation or other means. |
| Level 3 | Inputs that are both significant to the fair value measurement and unobservable. |

**Recently Issued Accounting Pronouncements**

In June 2011, the FASB issued Accounting Standards Update ( ASU ) No. 2011-05, *Presentation of Comprehensive Income.*  This ASU is designed to improve the comparability and transparency of other comprehensive income components. The guidance provides an option to present total comprehensive income, the components of net income and the components of other comprehensive income in a single continuous statement or two separate but consecutive statements. This ASU eliminates the option to present other comprehensive income components as part of the statement of changes in shareholders  equity. We have adopted this standard by presenting a separate consecutive statement of comprehensive income.

In February 2013, the FASB issued ASU 2013-02  *Comprehensive Income (Topic 220): Reporting Amounts Reclassified Out of Accumulated Other Comprehensive Income*  which will require new disclosures about items reclassified out of accumulated other comprehensive income. The new standard is required to be adopted in fiscal years, and interim periods within those years, beginning after December 15, 2012. This standard is not expected to have a material impact on us.

In September 2011, the FASB updated FASB ASC 350, *Intangibles  Goodwill and Other* to provide an entity the option, when evaluating goodwill and other assets for possible impairment, to first assess qualitative factors to determine whether the existence of events or circumstances leads to a determination that it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If, after completing this assessment, an entity determines it is not more likely than not that the fair value of a reporting unit is less than its carrying amount, then performing the two-step impairment test is unnecessary. We adopted this standard in the third quarter of 2012 and it did not have a material impact on us. This update became effective for us beginning January 1, 2012.

**3. ACQUISITIONS**

On February 12, 2010, we completed the acquisition of all the issued and outstanding stock of Concert Industries Corp. ( Concert ), a manufacturer of highly absorbent cellulose based airlaid non-woven materials, for cash totaling $231.1 million based on the currency exchange rates on the closing date, and net of post-closing working capital adjustments. Concert had operations located in Gatineau, Quebec, Canada and Falkenhagen, Brandenburg, Germany.

36

Table of Contents

The following summarizes the final purchase price allocation:

| *In thousands* | |
|---|---|
| Assets | |
| Cash | $ 2,792 |
| Accounts receivable | 24,120 |
| Inventory | 28,034 |
| Prepaid and other current assets | 4,625 |
| Plant, equipment and timberlands | 186,354 |
| Intangible assets | 5,040 |
| Deferred tax assets and other assets | 14,908 |
| Total | 265,873 |
| Liabilities | |
| Accounts payable and accrued expenses | 25,933 |
| Deferred tax liabilities | 5,336 |
| Other long term liabilities | 3,522 |
| Total | 34,791 |
| Total purchase price | $ 231,082 |

For purposes of allocating the total purchase price, assets acquired and liabilities assumed are recorded at their estimated fair market value. The allocation set forth above is based on management s estimate of the fair value using valuation techniques such as discounted cash flow models, appraisals and similar methodologies. The amount allocated to intangible assets represents the estimated value of customer sales contracts and relationships. Deferred tax assets reflect the estimated value of future tax deductions acquired in the transaction.

Our results of operations for 2010 include the results of Concert prospectively from the February 12, 2010 date of acquisition. All such results are reported herein as the Advanced Airlaid Materials business unit, a new reportable segment. Revenue and operating income of this operation included in our consolidated statements of income totaled $246.3 million and $18.0 million, respectively, in 2012, $252.0 million and $13.4 million, respectively, in 2011 and $193.5 million and $4.4 million, respectively, in 2010.

The unaudited pro forma results for 2010 include the amortization associated with the acquired intangible assets and interest expense associated with debt used to fund the acquisition, as well as fair value adjustments for plant, equipment and timberlands. To better reflect the combined operating results, material non-recurring charges directly attributable to the acquisition have been excluded. The unaudited pro forma financial information below is not necessarily indicative of either future results of operations or results that might have been achieved.

| *In thousands, except per share* | Year ended December 31 2010 |
|---|---|
| ***Pro forma*** | |
| Net sales | $ 1,480,980 |
| Net income | 69,116 |
| Diluted earnings per share | 1.49 |

**4. ENERGY AND RELATED SALES, NET**

We sell excess power generated by the Spring Grove, PA facility. Prior to the March 31, 2010 expiration of a long-term contract, all sales were at a fixed price. Subsequently, we sell excess power at prevailing market rates. We also sell renewable energy credits generated by the Spring Grove, PA and Chillicothe, OH facilities representing sales of certified credits earned related to burning renewable sources of energy such as black liquor and wood waste.

The following table summarizes this activity for each of the past three years:

| *In thousands* | **2012** | 2011 | 2010 |
|---|---|---|---|
| Energy sales | **$ 5,284** | $ 10,992 | $ 14,296 |

| | | | |
|---|---|---|---|
| Costs to produce | **(4,187)** | (9,319) | (10,403) |
| Net energy sales | **1,097** | 1,673 | 3,893 |
| Renewable energy credits | **5,903** | 7,671 | 6,760 |
| Total energy and related sales, net | **$ 7,000** | $ 9,344 | $ 10,653 |

Table of Contents

**5. GAIN ON DISPOSITIONS OF PLANT, EQUIPMENT AND TIMBERLANDS**

During 2012, 2011 and 2010, we completed the following sales of assets:

| *Dollars in thousands* | Acres | Proceeds | Gain |
|---|---|---|---|
| **2012** | | | |
| Timberlands | **4,830** | **$ 9,494** | **$ 9,203** |
| Other | **n/a** | **778** | **612** |
| Total | | **$ 10,272** | **$ 9,815** |
| **2011** | | | |
| Timberlands | 942 | $ 3,821 | $ 3,590 |
| Other | n/a | 670 | 360 |
| Total | | $ 4,491 | $ 3,950 |
| **2010** | | | |
| Timberlands | 164 | $ 387 | $ 373 |
| Other | n/a | 177 | 80 |
| | | $ 564 | $ 453 |

**6. EARNINGS PER SHARE**

The following table sets forth the details of basic and diluted earnings per share (EPS):

| | Year ended Decmber 31, | | |
|---|---|---|---|
| *In thousands, except per share* | 2012 | 2011 | 2010 |
| Net income | **$ 59,379** | $ 42,694 | $ 54,434 |
| Weighted average common shares outstanding used in basic EPS | **42,851** | 45,228 | 45,922 |
| Common shares issuable upon exercise of dilutive stock options and PSAs / RSUs | **821** | 566 | 452 |
| Weighted average common shares outstanding and common share equivalents used in diluted EPS | **43,672** | 45,794 | 46,374 |
| Earnings per share | | | |
| Basic | **$ 1.39** | $ 0.94 | $ 1.19 |
| Diluted | **1.36** | 0.93 | 1.17 |

The following table sets forth the potential common shares outstanding for stock options and restricted stock units that were not included in the computation of diluted EPS for the period indicated, because their effect would be anti-dilutive:

| | Year ended Decmber 31, | | |
|---|---|---|---|
| *in thousands* | **2012** | 2011 | 2010 |
| Potential common shares | **8** | 891 | 1,405 |

**7. INCOME TAXES**

Income taxes are recognized for the amount of taxes payable or refundable for the current year and deferred tax liabilities and assets for the future tax consequences of events that have been recognized in our consolidated financial statements or tax returns. The effects of income taxes are measured based on enacted tax laws and rates.

The provision/(benefit) for income taxes from operations consisted of the following:

| | Year Ended December 31 | | |
|---|---|---|---|
| *In thousands* | **2012** | 2011 | 2010 |
| Current taxes | | | |
| Federal | **$ 8,869** | $ 6,943 | $ (8,238) |

| | | | |
|---|---|---|---|
| State | **3,386** | (1,762) | (392) |
| Foreign | **9,516** | 2,637 | 4,540 |
| | **21,771** | 7,818 | (4,090) |
| Deferred taxes and other | | | |
| Federal | **(5,456)** | (3,908) | (17,530) |
| State | **(920)** | (286) | (131) |
| Foreign | **4,167** | 4,527 | 846 |
| | **(2,209)** | 333 | (16,815) |
| Income tax provision/(benefit) | **$ 19,562** | $ 8,151 | $ (20,905) |

The amounts set forth above for total deferred taxes and other included a deferred tax benefit of $2.3 million, $1.5 million and $17.6 million in 2012, 2011 and 2010, respectively. Other taxes totaled an expense of $0.1 million, $1.8 million, and $0.8 million in 2012, 2011 and 2010, respectively, associated with the deferred tax impact of uncertain tax positions.

The following are the domestic and foreign components of pretax income from operations:

| | Year Ended December 31 | | |
|---|---|---|---|
| *In thousands* | **2012** | 2011 | 2010 |
| United States | **$ 24,525** | $ (991) | $ 2,384 |
| Foreign | **54,416** | 51,836 | 31,145 |
| Total pretax income | **$ 78,941** | $ 50,845 | $ 33,529 |

A reconciliation between the income tax provision, computed by applying the statutory federal income tax rate of 35% to income before income taxes, and the actual income tax provision/(benefit) is as follows:

| | Year Ended December 31 | | |
|---|---|---|---|
| | **2012** | 2011 | 2010 |
| Federal income tax provision at statutory rate | **35.0%** | 35.0% | 35.0% |
| State income taxes, net of federal income tax benefit | **1.3** | 0.7 | 1.4 |
| Foreign income tax rate differential | **(3.9)** | (6.8) | (4.9) |
| Change in statutory tax rates | **(0.8)** | 0.9 | 1.5 |
| Tax credits | **(0.5)** | (2.0) | (7.8) |
| Change in unrecognized tax benefits, net | **0.4** | (11.6) | (12.4) |
| Cellulosic biofuel credit, net of incremental state tax and manufacturing deduction benefit | **(6.1)** | | (69.3) |
| Adjustment for prior year estimates | | | (6.8) |
| Valuation allowance | | 3.2 | |
| Other | **(0.6)** | (3.4) | 1.0 |
| Provision/(benefit) for income taxes | **24.8%** | 16.0% | (62.3)% |

38

**Table of Contents**

The sources of deferred income taxes were as follows at December 31:

| | **2012** | | 2011 | |
|---|---|---|---|---|
| *In thousands* | **Current Asset (Liability)** | **Non current Asset (Liability)** | Current Asset (Liability) | Non current Asset (Liability) |
| Reserves | **$ 6,871** | **$ 8,095** | $ 5,908 | $ 10,595 |
| Compensation | **3,332** | **5,034** | 3,481 | 5,064 |
| Post-retirement benefits | **1,285** | **22,642** | 1,325 | 18,467 |
| Property | | **(92,144)** | | (96,798) |
| Pension | **508** | **(14,681)** | 342 | (18,190) |
| Inventories | **1,447** | | 125 | |
| Other | **204** | **975** | (246) | 1,985 |
| Tax carryforwards | **5,218** | **43,409** | 3,313 | 47,294 |
| Subtotal | **18,865** | **(26,670)** | 14,248 | (31,583) |
| Valuation allowance | **(3,233)** | **(27,266)** | (1,586) | (25,946) |
| Total | **$ 15,632** | **$ (53,936)** | $ 12,662 | $ (57,529) |

Current and non-current deferred tax assets and liabilities are included in the following balance sheet captions:

| | December 31 | |
|---|---|---|
| *In thousands* | **2012** | 2011 |
| Prepaid expenses and other current assets | **$ 16,319** | $ 12,662 |
| Other long term assets | **8,110** | 12,262 |
| Other current liabilities | **687** | |
| Deferred income taxes | **62,046** | 69,791 |

At December 31, 2012 we had state and foreign tax net operating loss ( NOL ) carryforwards of $68.7 million and $247.9 million, respectively. These NOL carryforwards are available to offset future taxable income, if any. The state NOL carryforwards expire between 2014 and 2031; certain foreign NOL carryforwards expire between 2013 and 2032.

In addition, we had federal foreign tax credit carryforwards of $0.3 million, which expire in 2013, various state tax credit carryforwards totaling $0.4 million, which expire between 2014 and 2027, and foreign investment tax credits of $3.8 million which expire between 2019 and 2032.

We have established a valuation allowance of $30.5 million against the net deferred tax assets, primarily due to the uncertainty regarding the ability to utilize state and foreign tax NOL carryforwards and certain deferred foreign tax credits.

Tax credits and other incentives reduce tax expense in the year the credits are claimed. We recorded tax credits of $0.4 million, $1.0 million and $2.6 million in 2012, 2011 and 2010, respectively, related to research and development credits and the fuels tax credits.

At December 31, 2012 and 2011, unremitted earnings of subsidiaries outside the United States deemed to be permanently reinvested totaled $236.3 million and $197.4 million, respectively. Because the unremitted earnings of subsidiaries are deemed to be permanently reinvested as of December 31, 2012 and because we have no need for or plans to repatriate such earnings, no deferred tax liability has been recognized in our consolidated financial statements. The determination of additional taxes that have not been provided is not practicable.

In March 2010, our application to be registered as a cellulosic biofuel producer was approved by the Internal Revenue Service. The U.S. Internal Revenue Code provides a non refundable tax credit equal to $1.01 per gallon for taxpayers that produce cellulosic biofuel. In a memorandum issued in July 2010, the Internal Revenue Service issued guidance concluding that black liquor sold or used before January 1, 2010, qualifies for the cellulosic biofuel producer credit ( CBPC ) and no further certification of eligibility was needed.

In connection with the filing of our 2009 income tax return, we claimed $23.2 million, net of taxes, of CBPC. The CBPC claimed is attributable to black liquor produced and burned from January 1, 2009 through February 19, 2009, after which we began mixing black liquor and diesel fuel to qualify for alternative fuel mixture credits.

In 2012, we made the decision to convert a portion of the previously utilized refundable alternative fuel mixture credit, which was equal to $0.50 per gallon, to the non refundable CBPC. The conversion to the CBPC resulted in a net benefit for income taxes in 2012 of $4.0 million. During 2012, we amended our 2009 federal income tax return to claim the credit and this required us to return to the Internal Revenue Service $14.1 million, net of credits used to reduce estimated tax payments. We believe the credits are fully recognizable based on the Company s projections and economic analysis performed. Our ability to convert additional credits expires March 15, 2013.

As of December 31, 2012, 2011 and 2010, we had $30.4 million, $29.7 million and $38.7 million of gross unrecognized tax benefits, respectively. As of December 31, 2012, if such benefits were to be recognized, approximately $30.4 million would be recorded as a component of income tax expense, thereby affecting our effective tax rate.

Table of Contents

A reconciliation of the beginning and ending balances of the total amounts of gross unrecognized tax benefits is as follows:

| *In millions* | **2012** | 2011 | 2010 |
|---|---|---|---|
| Balance at January 1 | **$ 29.7** | $ 38.7 | $ 40.1 |
| Increases in tax positions for prior years | **1.4** | 0. 8 | 1.6 |
| Decreases in tax positions for prior years | **(1.0)** | (7.5) | (1.8) |
| Acquisition related: | | | |
| Purchase Accounting | | | 3.2 |
| Decrease for prior years(1) | | | (2.2) |
| Increases in tax positions for current year | **1.9** | 1.1 | 1.9 |
| Settlements | **(0.4)** | (0.1) | |
| Lapse in statutes of limitation | **(1.2)** | (3.3) | (4.1) |
| Balance at December 31 | **$ 30.4** | $ 29.7 | $ 38.7 |

(1) in connection with acquisition accounting for the Concert transaction, we recorded a $2.2 million reserve for an uncertain tax position and at the same time recorded a receivable from the seller due to an indemnification agreement. Prior to the end of 2010, a tax ruling was issued that eliminated this tax risk resulting in the elimination of both items.

We, or one of our subsidiaries, file income tax returns with the United States Internal Revenue Service, as well as various state and foreign authorities. The following table summarizes tax years that remain subject to examination by major jurisdiction:

| | Open Tax Years | |
|---|---|---|
| Jurisdiction | Examinations not yet initiated | Examination in progress |
| United States | | |
| Federal | 2009 2012 | N/A |
| State | 2008 2012 | 2004, 2006, 2008, 2009 |
| Canada (1) | 2010 2012 | 2007 2011 |
| Germany (1) | 2007, 2010 2012 | 2008 2010 |
| France | 2010 2012 | N/A |
| United Kingdom | 2009 2012 | N/A |
| Philippines | 2011 2012 | 2010 |

(1) includes provincial or similar local jurisdictions, as applicable.

The amount of income taxes we pay is subject to ongoing audits by federal, state and foreign tax authorities, which often result in proposed assessments. Management performs a comprehensive review of its global tax positions on a quarterly basis and accrues amounts for uncertain tax positions. Based on these reviews and the result of discussions and resolutions of matters with certain tax authorities and the closure of tax years subject to tax audit, reserves are adjusted as necessary. However, future results may include favorable or unfavorable adjustments to our estimated tax liabilities in the period the assessments are determined or resolved or as such statutes are closed. Due to potential for resolution of federal, state and foreign examinations, and the expiration of various statutes of limitation, it is reasonably possible our gross unrecognized tax benefits balance may

decrease within the next twelve months by a range of zero to $17.9 million. Substantially all of this range relates to tax positions taken in the U.S., the U.K. and in Germany.

We recognize interest and penalties related to uncertain tax positions as income tax expense. We recorded a benefit of $0.3 million during 2012, and in total, as of December 31, 2012, had recognized a liability for interest of $1.4 million. During 2011, we recorded a benefit of $2.1 million, and in total, as of December 31, 2011 had recognized a liability for interest of $1.7 million. During 2010, we accrued minimal interest expense and had recognized a liability for interest of $3.8 million at December 31, 2010. We did not record any penalties associated with uncertain tax positions during 2012, 2011 or 2010.

**8. STOCK-BASED COMPENSATION**

On April 29, 2009, our shareholders approved the P. H. Glatfelter Amended and Restated Long Term Incentive Plan (the LTIP ) authorizing, among other things, the issuance of up to 5,500,000 shares of Glatfelter common stock to eligible participants. The LTIP provides for the issuance of restricted stock units, restricted stock awards, non-qualified stock options, performance shares, incentive stock options and performance units. As of December 31, 2012, there were 1,708,079 shares of common stock available for future issuance under the LTIP.

Since the approval of the LTIP, we have issued to eligible participants restricted stock units, performance share awards and stock only stock appreciation rights ( SOSARs ).

**Restricted Stock Units ( RSUs ) and Performance Share Awards ( PSAs )** Awards of RSUs and PSAs are made under our LTIP. The vesting of RSUs is based solely on the passage of time, generally on a graded scale over a three, four, and five-year period. PSAs were first issued in March 2011 to members of senior management and cliff vest December 31, 2013, assuming the achievement of predetermined, three-year cumulative performance targets. The performance measures include a minimum, target and maximum performance level providing the grantees an opportunity to receive more or less shares than targeted depending on actual financial performance. For both RSUs and PSAs, the grant date fair value of the awards, which is equal to the closing price per common share on the date of the award, is used to determine the amount of expense to be recognized over the applicable service period. Settlement of RSUs and PSAs will be made in shares of our common stock.

Table of Contents

The following table summarizes RSU and PSA activity during the past three years:

| *Units* | **2012** | 2011 | 2010 |
|---|---|---|---|
| Balance January 1, | **788,088** | 579,801 | 564,037 |
| Granted | **209,021** | 251,031 | 203,889 |
| Forfeited | **(52,800)** | (28,254) | (37,368) |
| Shares delivered | **(96,630)** | (14,490) | (150,757) |
| Balance December 31, | **847,679** | 788,088 | 579,801 |

| *Dollars in thousands* | | | |
|---|---|---|---|
| Compensation expense | **$ 2,576** | $ 2,069 | $ 1,708 |

The amount granted in 2012 and 2011 includes 161,083 and 98,187 PSAs, respectively, exclusive of reinvested dividends. The weighted average grant fair value per unit for awards in 2012, 2011 and 2010 was $15.49, $12.47, and $13.24, respectively. As of December 31, 2012, unrecognized compensation expense for outstanding RSUs and PSAs totaled $4.0 million. The weighted average remaining period over which the expense will be recognized is 2.2 years.

**Stock Only Stock Appreciation Rights** The following table sets forth information related to outstanding SOSARS:

| | **2012** | | 2011 | | 2010 | |
|---|---|---|---|---|---|---|
| **SOSARS** | **Shares** | **Wtd Avg Exercise Price** | Shares | Wtd Avg Exercise Price | Shares | Wtd Avg Exercise Price |
| Outstanding at January 1, | **2,298,288** | **$ 12.35** | 2,061,877 | $ 12.28 | 1,762,020 | $ 11.84 |
| Granted | **364,114** | **15.58** | 345,290 | 12.56 | 470,520 | 13.77 |
| Exercised | **(500,074)** | **12.06** | | | | |
| Canceled / forfeited | **(40,874)** | **14.31** | (108,879) | 11.82 | (170,663) | 11.81 |
| Outstanding at December 31, | **2,121,454** | **12.93** | 2,298,288 | 12.35 | 2,061,877 | 12.28 |
| Exercisable at December 31, | **1,469,537** | **12.30** | 1,554,852 | 12.45 | 1,135,281 | 12.78 |
| Vested and expected to vest | **2,055,599** | | 2,076,341 | | 2,059,524 | |

| **SOSAR Grants** | **2012** | 2011 | 2010 |
|---|---|---|---|
| Weighted average grant date fair value per share | **$ 4.94** | $ 4.09 | $ 4.65 |
| Aggregate grant date fair value (in thousands) | **$ 1,797** | $ 1,412 | $ 2,179 |
| Black-Scholes assumptions | | | |
| Dividend yield | **2.31%** | 2.87% | 2.61% |
| Risk free rate of return | **1.02%** | 2.55% | 2.48% |
| Volatility | **41.48%** | 41.91% | 42.34% |
| Expected life | **6 yrs** | 6 yrs | 6 yrs |
| Compensation expense (in thousands) | **$ 1,448** | $ 1,564 | $ 2,254 |

Under terms of the SOSAR, the recipients received the right to receive a payment in the form of shares of common stock equal to the difference, if any, in the fair market value of one share of common stock at the time of exercising the SOSAR and the exercise price. The SOSARs vest ratably over a three year period. As of December 31, 2012, the intrinsic value of SOSARs vested and expected to vest totaled $9.4 million. The remaining weighted average contractual life of outstanding SOSARs was 6.7 years as of December 31, 2012.

Our LTIP also permits the issuance of nonqualified stock options; however, we have not issued any options since 2004. As of December 31, 2012, 22,500 stock options were outstanding with a weighted average exercise price of $11.29 per share. All options expire on the earlier of termination or, in some instances, a defined period subsequent to termination of employment, or ten years from the date of grant. The exercise price represents the quoted market price of Glatfelter common stock on the date of grant, or the average quoted market prices of Glatfelter common stock on the first day before and after the date of grant for which quoted market price information was available if such information was not available on the date of grant. As of December 31, 2012, the intrinsic value of outstanding stock options totaled $0.1 million.

Table of Contents

## 9. RETIREMENT PLANS AND OTHER POST-RETIREMENT BENEFITS

We provide non-contributory retirement benefits under both funded and unfunded plans to all U.S. employees and to certain non-U.S. employees. U.S. benefits are based on either a final average pay formula or a cash balance formula for salaried employees, and on a unit-benefit formula for bargained hourly employees. Non-U.S. benefits are based, in the case of certain plans, on average salary and years of service and, in the case of other plans, on a fixed amount for each year of service. U.S. plan provisions and funding meet the requirements of the Employee Retirement Income Security Act of 1974. We use a December 31-measurement date for all of our defined benefit plans.

We also provide certain health care benefits to eligible U.S.-based retired employees and exclude all salaried employees hired after January 1, 2008. These benefits include a comprehensive medical plan for retirees prior to age 65 and fixed supplemental premium payments to certain retirees over age 65 to help defray the costs of Medicare. Claims are paid as reported.

| | Pension Benefits | | Other Benefits | |
|---|---|---|---|---|
| *In millions* | **2012** | 2011 | **2012** | 2011 |
| **Change in Benefit Obligation** | | | | |
| Balance at beginning of year | **$ 470.2** | $ 434.3 | **$ 56.8** | $ 58.5 |
| Service cost | **11.3** | 10.3 | **2.8** | 2.9 |
| Interest cost | **23.0** | 24.2 | **2.4** | 2.8 |
| Plan amendments | **5.5** | 2.0 | | |
| Participant contributions | | | **1.4** | 1.7 |
| Actuarial (gain)/loss | **46.7** | 33.8 | **4.2** | (4.4) |
| Benefits paid | **(28.3)** | (34.4) | **(4.6)** | (4.7) |
| Balance at end of year | **$ 528.4** | $ 470.2 | **$ 63.0** | $ 56.8 |
| **Change in Plan Assets** | | | | |
| Fair value of plan assets at beginning of year | **$ 498.2** | $ 526.4 | **$ 5.3** | $ 6.2 |
| Actual (loss) return on plan assets | **68.1** | (2.6) | **0.6** | |
| Total contributions | **1.8** | 8.8 | **4.6** | 3.8 |
| Benefits paid | **(28.3)** | (34.4) | **(4.6)** | (4.7) |
| Intra plan transfers | **5.9** | | **(5.9)** | |
| Fair value of plan assets at end of year | **545.7** | 498.2 | | 5.3 |
| Funded status at end of year | **$ 17.3** | $ 28.0 | **$ (63.0)** | $ (51.5) |

The amount set forth for intra plan transfers represents assets contributed to the pension plan from a post-retirement medical plan sub-account previously established pursuant to Section 420 of the Internal Revenue Code. Benefits due under the post-retirement medical plan continue to be paid for by us.

Amounts recognized in the consolidated balance sheets consist of the following as of December 31:

| | Pension Benefits | | Other Benefits | |
|---|---|---|---|---|
| *In millions* | **2012** | 2011 | **2012** | 2011 |
| Other long-term assets | **$ 53.7** | $ 59.8 | **$** | $ |
| Current liabilities | **(2.0)** | (1.8) | **(4.2)** | (3.4) |
| Other long-term liabilities | **(34.4)** | (30.0) | **(58.8)** | (48.1) |
| Net amount recognized | **$ 17.3** | $ 28.0 | **$ (63.0)** | $ (51.5) |

The components of amounts recognized as Accumulated other comprehensive income consist of the following on a pre-tax basis:

| | Pension Benefits | | Other Benefits | |
|---|---|---|---|---|
| *In millions* | **2012** | 2011 | **2012** | 2011 |
| Prior service cost/(credit) | **$ 17.9** | $ 14.9 | **$ (1.9)** | ($ 2.8) |
| Net actuarial loss | **237.6** | 234.0 | **12.6** | 9.2 |

The accumulated benefit obligation for all defined benefit pension plans was $507.4 million and $451.7 million at December 31, 2012 and 2011, respectively.

The weighted-average assumptions used in computing the benefit obligations above were as follows:

| | Pension Benefits | | Other Benefits | |
|---|---|---|---|---|
| | **2012** | 2011 | **2012** | 2011 |
| Discount rate benefit obligation | **4.28%** | 5.09% | **3.58%** | 4.45% |
| Future compensation growth rate | **4.00** | 4.00 | | |

The discount rates set forth above were estimated based on the modeling of expected cash flows for each of our benefit plans and selecting a portfolio of high-quality debt instruments with maturities matching the respective cash flows of each plan. The resulting discount rates ranged from 3.50% to 4.51% for pension plans and ranged from 3.02% to 3.69% for other benefit plans.

Information for pension plans with an accumulated benefit obligation in excess of plan assets was as follows:

| *In millions* | **2012** | 2011 |
|---|---|---|
| Projected benefit obligation | **$ 36.4** | $ 31.8 |
| Accumulated benefit obligation | **32.0** | 27.9 |
| Fair value of plan assets | | |

Table of Contents

Net periodic benefit cost (income) includes the following components:

| | Year Ended December 31 | | |
|---|---|---|---|
| *In millions* | **2012** | 2011 | 2010 |
| **Pension Benefits** | | | |
| Service cost | **$ 11.3** | $ 10.3 | $ 9.5 |
| Interest cost | **23.0** | 24.2 | 23.9 |
| Expected return on plan assets | **(42.2)** | (42.0) | (40.3) |
| Amortization of prior service cost | **2.5** | 2.6 | 2.5 |
| Amortization of actuarial loss | **17.0** | 13.3 | 13.6 |
| One-time settlement charge | | 2.0 | |
| Total net periodic benefit cost | **$ 11.6** | $ 10.4 | $ 9.2 |
| **Other Benefits** | | | |
| Service cost | **$ 2.8** | $ 2.9 | $ 2.9 |
| Interest cost | **2.4** | 2.8 | 3.4 |
| Expected return on plan assets | **(0.5)** | (0.5) | (0.5) |
| Amortization of prior service cost/(credit) | **(0.9)** | (1.2) | (1.2) |
| Amortization of actuarial loss | **0.7** | 0.9 | 1.5 |
| Total net periodic benefit cost | **$ 4.5** | $ 4.9 | $ 6.1 |

In connection with the December 31, 2010 retirement of our former chief executive officer and the lump-sum distribution in July 2011 of accrued pension benefits due to him, we recorded a $2.0 million one-time pension settlement charge in 2011.

The prior service cost and actuarial net (gain) loss for our defined benefit pension plans that will be amortized from accumulated other comprehensive income (loss) into our results of operations as a component of net periodic benefit cost over the next fiscal year are $3.1 million and $21.3 million, respectively. The comparable amounts of expected amortization for other benefit plans are a credit of $0.5 million and expense of $0.8 million, respectively.

Other changes in plan assets and benefit obligations recognized in other comprehensive income (loss) were as follows:

| | Year Ended December 31 | |
|---|---|---|
| *In millions* | **2012** | 2011 |
| **Pension Benefits** | | |
| Actuarial loss | **$ 20.6** | $ 76.5 |
| Prior service cost | **5.5** | 2.1 |
| Amortization of prior service cost | **(2.5)** | (2.6) |
| Amortization of actuarial losses | **(17.0)** | (13.3) |
| Total recognized in other comprehensive loss | **6.6** | 62.7 |
| Total recognized in net periodic benefit cost and other comprehensive loss | **$ 18.2** | $ 73.1 |
| **Other Benefits** | | |
| Actuarial (gain) loss | **$ 4.0** | $ (3.8) |
| Amortization of prior service cost | **0.9** | 1.2 |
| Amortization of actuarial losses | **(0.7)** | (0.9) |
| Total recognized in other comprehensive (income) loss | **4.2** | (3.5) |
| Total recognized in net periodic benefit cost and other comprehensive loss | **$ 8.7** | $ 1.4 |

The weighted-average assumptions used in computing the net periodic benefit (income) cost information above were as follows:

| | Year Ended December 31 | | |
|---|---|---|---|
| | **2012** | 2011 | 2010 |
| **Pension Benefits** | | | |
| Discount rate benefit expense | **5.09%** | 5.81% | 6.10% |
| Future compensation growth rate | **4.00** | 4.00 | 4.00 |
| Expected long-term rate of return on plan assets | **8.50** | 8.50 | 8.50 |
| **Other Benefits** | | | |
| Discount rate benefit expense | **4.45%** | 5.12% | 5.90% |
| Expected long-term rate of return on plan assets | **8.50** | 8.50 | 8.50 |

To develop the expected long-term rate of return assumption, we considered the historical returns and the future expected returns for each asset class, as well as the target asset allocation of the pension portfolio.

Assumed health care cost trend rates used to determine benefit obligations at December 31 were as follows:

| | **2012** | 2011 |
|---|---|---|
| Health care cost trend rate assumed for next year | **7.68%** | 7.90% |
| Rate to which the cost trend rate is assumed to decline (the ultimate trend rate) | **4.50** | 4.50 |
| Year that the rate reaches the ultimate rate | **2028** | 2028 |

Assumed health care cost trend rates have a significant effect on the amounts reported for health care plans. A one percentage-point change in assumed health care cost trend rates would have the following effects:

| | **One Percentage Point** | |
|---|---|---|
| *In millions* | **Increase** | **Decrease** |
| Effect on: | | |
| Post-retirement benefit obligation | $ 4.9 | $ 4.4 |
| Total of service and interest cost components | 0.6 | 0.5 |

**Plan Assets** All pension plan assets in the U.S. are invested through a single master trust fund. The strategic asset allocation for this trust fund is selected by management, reflecting the results of comprehensive asset and liability modeling. The general principles guiding U.S. pension asset investment policies are those embodied in the Employee Retirement Income Security Act of 1974 (ERISA). These principles include discharging our investment responsibilities for the exclusive benefit of plan participants and in accordance with the prudent expert standard and other ERISA rules and regulations. We establish strategic asset allocation percentage targets and appropriate benchmarks for significant asset classes with the aim of achieving a prudent balance between return and risk.

Investments and decisions will be made solely in the interest of the Plan s participants and beneficiaries, and for

**Table of Contents**

the exclusive purpose of providing benefits accrued thereunder. The primary goal of the Plan is to ensure the solvency of the Plan over time and thereby meet its distribution objectives. Plan assets will be diversified. All investments in the Plan will be made in accordance with ERISA and other applicable statutes.

Risk is minimized by diversification by asset class, by style of each manager and by sector and industry limits when applicable. The target allocation for the Plan assets are:

| | |
|---|---|
| Domestic Equity | |
| Large cap | **39%** |
| Small and mid cap | **13** |
| International equity | **13** |
| Real Estate Investment Trusts (REIT) | **5** |
| Fixed income, cash and cash equivalents | **30** |

Diversification is achieved by:

i. placing restrictions on the percentage of equity investments in any one company, percentage of investment in any one industry, limiting the amount of assets placed with any one manager; and

ii. setting targets for duration of fixed income securities, maintaining a certain level of credit quality, and limiting the amount of investment in a single security and in non-investment grade paper.

A formal asset allocation review is done periodically to ensure that the Plan has an appropriate asset allocation based on the Plan s projected benefit obligations. The target return for each equity and fixed income manager will be one that places the manager s performance in the top 40% of its peers and on a gross basis, exceeds that of the manager s respective benchmark index. The target return for cash and cash equivalents is a return that at least equals that of the 90-day T-bills.

The Investment Policy statement lists specific categories of securities or activities that are prohibited including options, futures, commodities, hedge funds, limited partnerships, and our stock.

The table below presents the fair values of our benefit plan assets by level within the fair value hierarchy, as described in Note 2:

| | Fair Value Measurements at December 31, 2012 | | | |
|---|---|---|---|---|
| *In millions* | Total | Level 1 | Level 2 | Level 3 |
| Domestic Equity | | | | |
| Large cap | **$ 169.6** | **$ 169.6** | **$** | **$** |
| Small and mid cap | **65.7** | **65.7** | | |
| Other | **1.1** | **0.8** | **0.3** | |
| International equity | **100.3** | **61.9** | **38.4** | |
| REIT | **25.4** | **25.4** | | |
| Fixed income | **164.9** | **27.2** | **137.7** | |
| Cash and equivalents | **18.7** | | **18.7** | |
| Total | **$ 545.7** | **$ 350.6** | **$ 195.1** | **$** |

| | Fair Value Measurements at December 31, 2011 | | | |
|---|---|---|---|---|
| *In millions* | Total | Level 1 | Level 2 | Level 3 |
| Domestic Equity | | | | |
| Large cap | $ 164.5 | $ 164.5 | $ | $ |
| Small and mid cap | 57.7 | 57.7 | | |
| Other | 0.6 | 0.5 | 0.1 | |
| International equity | 79.7 | 48.3 | 31.4 | |

| | | | | |
|---|---|---|---|---|
| REIT | 26.4 | 26.4 | | |
| Fixed income | 157.3 | 83.4 | 73.9 | |
| Cash and equivalents | 17.3 | | 17.3 | |
| Total | $ 503.5 | $ 380.8 | $ 122.7 | $ |

**Cash Flow** We were not required to make contributions to our qualified pension plan in 2012 nor do we expect to make any to this plan in 2013. Benefit payments expected to be made in 2013 under our non-qualified pension plans and other benefit plans are summarized below:

| *In thousands* | |
|---|---|
| Nonqualified pension plans | **$ 2,014** |
| Other benefit plans | **4,238** |

The following benefit payments under all pension and other benefit plans, and giving effect to expected future service, as appropriate, are expected to be paid:

| *In thousands* | Pension Benefits | Other Benefits |
|---|---|---|
| 2013 | **$ 32,465** | **$ 4,238** |
| 2014 | **32,135** | **4,557** |
| 2015 | **32,179** | **4,574** |
| 2016 | **31,977** | **4,823** |
| 2017 | **31,986** | **5,104** |
| 2018 through 2022 | **156,439** | **26,328** |

**Defined Contribution Plans** We maintain 401(k) plans for certain hourly and salaried employees. Employees may contribute up to 50% of their earnings, subject to certain restrictions. We will match a portion of the employee s contribution, subject to certain limitations, in the form of shares of Glatfelter common stock out of treasury. The expense associated with our 401(k) match was $1.7 million, $1.3 million and $1.0 million in 2012, 2011 and 2010, respectively.

Table of Contents

## 10. INVENTORIES

Inventories, net of reserves were as follows:

| *In thousands* | **2012** | 2011 |
|---|---|---|
| Raw materials | **$ 61,084** | $ 57,547 |
| In-process and finished | **102,331** | 93,096 |
| Supplies | **58,951** | 56,064 |
| Total | **$ 222,366** | $ 206,707 |

We value all of our U.S. inventories, excluding supplies, on the LIFO method. If we had valued these inventories using the first-in, first-out method, inventories would have been $22.4 million and $22.1 million higher than reported at December 31, 2012 and 2011, respectively. During 2011, we liquidated certain LIFO inventories, the effect of which did not have a significant impact on results of operations.

## 11. PLANT, EQUIPMENT AND TIMBERLANDS

Plant, equipment and timberlands at December 31 were as follows:

| *In thousands* | **2012** | 2011 |
|---|---|---|
| Land and buildings | **$ 194,541** | $ 186,846 |
| Machinery and equipment | **1,158,245** | 1,102,709 |
| Furniture, fixtures, and other | **122,425** | 117,082 |
| Accumulated depreciation | **(915,777)** | (850,255) |
| | **559,434** | 556,382 |
| Construction in progress | **52,782** | 34,576 |
| Asset retirement obligation, net | **6,374** | 7,968 |
| Timberlands, less depletion | **2,596** | 3,024 |
| Total | **$ 621,186** | $ 601,950 |

## 12. GOODWILL AND INTANGIBLE ASSETS

The following table sets forth information with respect to goodwill and other intangible assets which are recorded in the caption Other long-term assets in the accompanying consolidated balance sheets:

| | December 31 | |
|---|---|---|
| *In thousands* | **2012** | 2011 |
| Goodwill Composite Fibers | **$16,601** | $ 16,161 |
| Specialty Papers | | |
| Customer relationships | **$ 6,155** | $ 6,155 |
| Composite Fibers | | |
| Technology and related | **4,365** | 4,174 |
| Customer relationships and related | **1,872** | 1,790 |
| Advanced Airlaid Materials | | |
| Technology and related | **1,579** | 1,560 |
| Customer relationships and related | **3,300** | 3,238 |
| Total intangibles | **17,271** | 16,917 |
| Accumulated amortization | **(8,970)** | (7,027) |
| Net intangibles | **$ 8,301** | $ 9,890 |

The change in goodwill was due to foreign currency translation adjustments. Other than non-amortizable goodwill, intangible assets are amortized on a straight-line

basis. Customer relationships are amortized over periods ranging from 3 years to 14 years and technology and related intangible assets are amortized over periods ranging from 14 years to 20 years. The following table sets forth information pertaining to amortization of intangible assets:

| *In thousands* | **2012** | 2011 |
|---|---|---|
| Aggregate amortization expense | **$ 1,778** | $ 1,858 |
| Estimated amortization expense | | |
| 2013 | **1,314** | |
| 2014 | **1,314** | |
| 2015 | **1,314** | |
| 2016 | **852** | |
| 2017 | **699** | |

The remaining weighted average useful life of intangible assets was 8.2 years at December 31, 2012.

## 13. OTHER LONG-TERM ASSETS

Other long-term assets consist of the following:

| | December 31 | |
|---|---|---|
| *In thousands* | **2012** | 2011 |
| Pension | **$ 53,734** | $ 59,821 |
| Goodwill and intangibles | **24,902** | 26,051 |
| Other | **24,305** | 26,690 |
| Total | **$ 102,941** | $ 112,562 |

## 14. OTHER CURRENT LIABILITIES

Other current liabilities consist of the following:

| | December 31 | |
|---|---|---|
| *In thousands* | **2012** | 2011 |
| Accrued payroll and benefits | **$ 50,637** | $ 48,654 |
| Other accrued compensation and retirement benefits | **8,977** | 6,253 |
| Income taxes payable | **2,656** | 3,543 |
| Accrued rebates | **11,330** | 10,839 |
| Other accrued expenses | **39,889** | 28,309 |
| Total | **$ 113,489** | $ 97,598 |

## 15. LONG-TERM DEBT

Long-term debt is summarized as follows:

| | December 31 | |
|---|---|---|
| *In thousands* | **2012** | 2011 |
| Revolving credit facility, due Nov. 2016 | **$** | $ 27,000 |
| 5.375% Notes, due Nov 2020 | **250,000** | |
| 7.125% Notes, due May 2016 | | 200,000 |
| Total long-term debt | **250,000** | 227,000 |
| Less current portion | | |
| Long-term debt, net of current portion | **$ 250,000** | $ 227,000 |

On November 21, 2011, we entered into an amendment to our revolving credit agreement with a consortium of banks (the Revolving Credit Facility ) which increased the amount available for borrowing to $350

Table of Contents

million, extended the maturity of the facility to November 21, 2016, and instituted a lower interest rate pricing grid.

For all U.S. dollar denominated borrowings under the Revolving Credit Facility, the borrowing rate is, at our option, (a) the bank s base rate which is equal to the greater of i) the prime rate; ii) the federal funds rate plus 50 basis points plus an applicable spread ranging from 25 basis points to 125 basis points based on our corporate credit ratings determined by Standard & Poor s Rating Services and Moody s Investor Service, Inc. (the Corporate Credit Rating ); or iii) the daily Euro-rate plus 100 basis points; or (b) the daily Euro-rate plus an applicable margin ranging from 125 basis points to 225 basis points based on the Corporate Credit Rating. For non-US dollar denominated borrowings, interest is based on (b) above.

The Revolving Credit Facility contains a number of customary covenants for financings of this type that, among other things, restrict our ability to dispose of or create liens on assets, incur additional indebtedness, repay other indebtedness, limits certain intercompany financing arrangements, make acquisitions and engage in mergers or consolidations. We are also required to comply with specified financial tests and ratios including: i) maximum net debt to earnings before interest, taxes, depreciation and amortization ( EBITDA ) ratio; ii) a consolidated EBITDA to interest expense ratio; and iii) beginning December 31, 2015, a minimum liquidity ratio. A breach of these requirements would give rise to certain remedies under the Revolving Credit Facility, among which are the termination of the agreement and accelerated repayment of the outstanding borrowings plus accrued and unpaid interest under the credit facility.

On October 3, 2012, we completed a private placement offering of $250.0 million aggregate principal amount of 5.375% Senior Notes due 2020 (the 5.375% Notes ). The 5.375% Notes are fully and unconditionally guaranteed, jointly and severally, by PHG Tea Leaves, Inc., Mollanvick, Inc., The Glatfelter Pulp Wood Company, and Glatfelter Holdings, LLC (the Guarantors ). The net proceeds from this offering totaled approximately $245.1 million, after deducting the commissions and other fees and expenses relating to the offering and were used to tender and call $200.0 million aggregate principal amount of our outstanding 7.125% notes due November 2016, plus the payment of the applicable redemption premium and accrued interest. We used the remaining net proceeds to repay amounts outstanding under our revolving credit facility and for general corporate purposes. Pursuant to the redemption provisions contained in the 7.125% Notes

Indenture, we redeemed all of the 7.125% Notes at 102.375% of par. The $4.8 million redemption premium is reported under the caption other non-operating expenses other-net in the accompanying consolidated statements of income. The write-off of the related unamortized deferred financing fees totaled $1.9 million and is reported under the caption Interest expense in the accompanying consolidated statements of income.

Unamortized deferred debt issuance costs incurred in connection with the offering of the 5.375% Notes totaled $4.8 million and are reported under the caption Other assets in the accompanying consolidated balance sheets. The deferred costs are being amortized on a straight line basis over the life of the 5.375% Notes.

Interest on the 5.375% Notes will be payable semiannually in arrears on April 15 and October 15, commencing on April 15, 2013.

The 5.375% Notes are redeemable, in whole or in part, at anytime on or after October 15, 2016 at the redemption prices specified in the applicable Indenture. Prior to October 15, 2016, we may redeem some or all of the Notes at a make-whole premium as specified in the Indenture. These notes and the guarantees of the notes are senior obligations of the Company and the Guarantors, respectively, rank equally in right of payment with future senior indebtedness of the Company and the Guarantors and will mature on October 15, 2020.

The 5.375% Notes contain cross default provisions that could result in all such notes becoming due and payable in the event of a failure to repay debt outstanding under the Revolving Credit Agreement at maturity or a default under the Revolving Credit Agreement that accelerates the debt outstanding thereunder. As of December 31, 2012, we met all of the requirements of our debt covenants.

The following schedule sets forth the maturity of our long-term debt during the indicated year.

| *In thousands* | |
|---|---|
| 2013 | **$** |
| 2014 | |
| 2015 | |
| 2016 | |
| 2017 | |
| Thereafter | **$ 250,000** |

P. H. Glatfelter Company guarantees all debt obligations of its subsidiaries. All such obligations are recorded in these consolidated financial statements.

As of December 31, 2012 and 2011, we had $5.2 million and $4.6 million, respectively, of letters of credit

46

Table of Contents

issued to us by certain financial institutions. The letters of credit, which reduce amounts available under our revolving credit facility, primarily provide financial assurances for the benefit of certain state workers compensation insurance agencies in conjunction with our self-insurance program. We bear the credit risk on this amount to the extent that we do not comply with the provisions of certain agreements. No amounts are outstanding under the letters of credit.

**16. ASSET RETIREMENT OBLIGATION**

During 2008, we recorded $11.5 million, net present value, of asset retirement obligations related to the legal requirement to close several lagoons at the Spring Grove, PA facility. Historically, lagoons were used to dispose of residual waste material. Closure of the lagoons, which is expected to be completed over the next four years, will be accomplished by filling the lagoons, installing a non-permeable liner which will be covered with soil to construct the required cap over the lagoons. The amount referred to above, in addition to upward revisions, were accrued with a corresponding increase in the carrying value of the property, equipment and timberlands caption on the consolidated balance sheet. The amount capitalized is being amortized as a charge to operations on the straight-line basis in relation to the expected closure period.

Following is a summary of the reserve for asset retirement obligations for the periods indicated:

| *In thousands* | **2012** | 2011 |
|---|---|---|
| Balance at Jan. 1, | **$ 9,679** | $ 9,717 |
| Upward revision | | 611 |
| Accretion | **458** | 550 |
| Payments | **(1,255)** | (1,199) |
| Balance at Dec. 31, | **$ 8,882** | $ 9,679 |

At December 31, 2012 and 2011, $3.6 million and $1.5 million, respectively, is recorded in the accompanying consolidated balance sheets under the caption Other current liabilities and the balance is recorded under the caption Other long-term liabilities.

**17. FAIR VALUE OF FINANCIAL INSTRUMENTS**

The amounts reported on the consolidated balance sheets for cash and cash equivalents, accounts receivable

and short-term debt approximate fair value. The following table sets forth the carrying value and fair value of long-term debt as of December 31:

| | **2012** | | 2011 | |
|---|---|---|---|---|
| *In thousands* | Carrying Value | Fair Value | Carrying Value | Fair Value |
| Fixed-rate bonds | **$ 250,000** | **$ 260,340** | $ 200,000 | $ 204,000 |
| Variable rate debt | | | 27,000 | 27,000 |
| Total | **$ 250,000** | **$ 260,340** | $ 227,000 | $ 231,000 |

As of December 31, 2012, we had $250.0 million of 5.375% fixed rate debt, and as of December 31, 2011, we had $200.0 million of 7.125% fixed rate debt. These bonds are publicly registered, but thinly traded. Accordingly, the values set forth above are based on debt instruments with similar characteristics (Level 2). The fair value of financial derivatives is set forth below in Footnote 18.

**18. FINANCIAL DERIVATIVES AND HEDGING ACTIVITIES**

As part of our overall risk management practices, we enter into financial derivatives primarily designed to either i) hedge foreign currency risks associated with forecasted transactions cash flow hedges ; or ii) mitigate the impact that changes in currency exchange rates have on intercompany financing transactions and foreign currency denominated receivables and payables foreign currency hedges.

***Derivatives Designated as Hedging Instruments Cash Flow Hedges*** In 2011, we began to use currency forward contracts as cash flow hedges to manage our exposure to fluctuations in the currency exchange rates on certain forecasted production costs expected to be incurred over a maximum of twelve months. Currency forward contracts involve fixing the EUR-USD exchange rate or USD-CAD for delivery of a specified amount of foreign currency on a specified date.

We designate certain currency forward contracts as cash flow hedges of forecasted raw material purchases or other production costs with exposure to changes in foreign currency exchange rates. The effective portion of changes in the fair value of derivatives designated and that qualify as cash flow hedges of foreign exchange risk is deferred as a component of accumulated other comprehensive income in the accompanying consolidated balance sheet and is subsequently reclassified into cost of products sold in the period that inventory produced using the hedged transaction affects earnings. The ineffective portion of the

Table of Contents

change in fair value of the derivative is recognized directly to earnings and reflected in the accompanying consolidated statement of income as non-operating income (expense) under the caption Other-net.

We had the following outstanding derivatives that were used to hedge foreign exchange risks associated with forecasted transactions and designated as hedging instruments:

| *In thousands* | **2012** | 2011 |
|---|---|---|
| Derivative | Buy Notional | |
| Sell / Buy | | |
| Euro / U.S. dollar | **27,003** | 22,730 |
| U.S. dollar / Canadian dollar | **12,369** | 11,019 |

These contracts have maturities of twelve months or less.

***Derivatives Not Designated as Hedging Instruments Foreign Currency Hedges*** We also enter into forward foreign exchange contracts to mitigate the impact changes in currency exchange rates have on balance sheet monetary assets and liabilities. None of these contracts are designated as hedges for financial accounting purposes and, accordingly, changes in value of the foreign exchange forward contracts and in the offsetting underlying on-balance-sheet transactions are reflected in the accompanying statement of operations under the caption Other net.

| *In thousands* | **2012** | 2011 |
|---|---|---|
| Derivative | Sell Notional | |
| Sell / Buy | | |
| Euro / U.S. dollar | **13,000** | 25,500 |
| Euro / British Pound | **4,000** | |
| Canadian dollar / U.S. dollar | **2,000** | |
| U.S. dollar / Euro | **2,000** | |
| Philippine peso / U.S. dollar | | 150,000 |

These contracts have maturities of one month from the date originally entered into.

***Fair Value Measurements***

The following table summarizes the fair values of derivative instruments as of December 31 for the year

indicated and the line items in the accompanying consolidated balance sheet where the instruments are recorded:

| *In thousands* | **2012** | 2011 | **2012** | 2011 |
|---|---|---|---|---|
| Balance sheet caption | Prepaid and Other Current Assets | | Other Current Liabilities | |
| ***Designated as hedging:*** | | | | |
| Forward foreign currency exchange contracts | **$ 107** | $1,520 | **$751** | |
| ***Not designated as hedging:*** | | | | |
| Forward foreign currency exchange contracts | **$ 159** | $338 | **$16** | $ 15 |

The amounts set forth in the table above represent the net asset or liability giving effect to rights of offset with each counterparty.

The following table summarizes the amount of income or loss from derivative instruments recognized in our results of operations for the periods indicated and the line items in the accompanying consolidated statements of income where the results are recorded:

| *In thousands* | **2012** | 2011 | 2010 |
|---|---|---|---|
| ***Designated as hedging:*** | | | |
| Forward foreign currency exchange contracts: | | | |

| | | | |
|---|---|---|---|
| Effective portion cost of products sold | **$ 2,183** | $ 174 | $ |
| Ineffective portion other net | **311** | 165 | |
| ***Not designated as hedging**:* | | | |
| Forward foreign currency exchange contracts: | | | |
| Other net | **$ (696)** | $ (686) | $ (1,047) |

The impact of activity not designated as hedging was substantially all offset by the remeasurement of the underlying on-balance sheet item.

The fair value hierarchy consists of three broad levels, which gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). The three levels of the fair value hierarchy are described in Note 2.

The fair values of the foreign exchange forward contracts are considered to be Level 2. Foreign currency forward contracts are valued using foreign currency forward and interest rate curves. The fair value of each contract is determined by comparing the contract rate to the forward rate and discounting to present value. Contracts in a gain position are recorded in the consolidated balance sheet under the caption Prepaid and other current assets and

Table of Contents

the value of contracts in a loss position is recorded under the caption Other current liabilities.

A rollforward of fair value amounts recorded as a component of accumulated other comprehensive income is as follows:

| *In thousands* | **2012** | 2011 |
|---|---|---|
| Balance at Jan. 1 | **$ 1,649** | $ |
| Deferred (loss) gains on cash flow hedges | **(65)** | 1,823 |
| Reclassified to earnings | **(2,183)** | (174) |
| Balance at Dec. 31 | **$ (599)** | $ 1,649 |

We expect substantially all of the amounts recorded as a component of accumulated other comprehensive income will be realized in results of operations within the next twelve months and the amount ultimately recognized will vary depending on actual market rates.

Credit risk related to derivative activity arises in the event a counterparty fails to meet its obligations to us. This exposure is generally limited to the amounts, if any, by which the counterparty s obligations exceed our obligation to them. Our policy is to enter into contracts only with financial institutions which meet certain minimum credit ratings.

**19. SHAREHOLDERS EQUITY**

The following table summarizes outstanding shares of common stock:

| | Year Ended December 31, | | |
|---|---|---|---|
| *In thousands* | **2012** | 2011 | 2010 |
| Shares outstanding at beginning of year | **42,650** | 45,976 | 45,706 |
| Shares repurchased | **(374)** | (3,505) | |
| Treasury shares issued for: | | | |
| Restricted stock awards | **76** | 14 | 112 |
| 401(k) plan | **152** | 143 | 132 |
| Director compensation | | 12 | 12 |
| Employee stock options exercised | **280** | 10 | 14 |
| Shares outstanding at end of year | **42,784** | 42,650 | 45,976 |

**20. SHARE REPURCHASES**

In May 2012, our Board of Directors authorized a new share repurchase program for up to $25.0 million of our outstanding common stock, exclusive of commissions. The following table summarizes share repurchases through December 31, 2012, made under this program:

| | shares | *(thousands)* |
|---|---|---|
| Authorized amount | **n/a** | **$ 25,000** |
| Repurchases | **291,120** | **(4,462)** |
| Remaining authorization | | **$ 20,538** |

In April 2011, our Board of Directors authorized a share repurchase program for up to $50.0 million of our outstanding common stock, exclusive of commissions, all of which has been used, including 82,533 shares at a cost of $1.2 million repurchased under this program in the first quarter of 2012.

**21. COMMITMENTS, CONTINGENCIES AND LEGAL PROCEEDINGS**

**Contractual Commitments** The following table summarizes the minimum annual payments due on noncancelable operating leases and other similar contractual obligations having initial or remaining terms in excess of one year:

| *In thousands* | Leases | Other |
|---|---|---|
| 2013 | $ 4,928 | $ 133,788 |
| 2014 | 3,373 | 40,595 |
| 2015 | 2,798 | 27,728 |
| 2016 | 2,329 | 1,039 |
| 2017 | 2,078 | 507 |
| thereafter | 5,595 | |

Other contractual obligations primarily represent minimum purchase commitments under energy and pulp wood supply contracts and other purchase obligations.

At December 31, 2012, required minimum annual payments due under operating leases and other similar contractual obligations aggregated $21.1 million and $203.7 million, respectively.

**Fox River Neenah, Wisconsin**

***Background*** We have significant uncertainties associated with environmental claims arising out of the presence of polychlorinated biphenyls ( PCBs ) in sediments in the lower Fox River, on which our former Neenah facility was located, and in the Bay of Green Bay Wisconsin ( Site ). The United States, the State of Wisconsin, and two Indian tribes (collectively, the Governments ) seek to require (a) a cleanup of the Site ( response actions ), (b) reimbursement of cleanup costs ( response costs ), and (c) natural resource damages ( NRDs ). They claim that we, together with seven other entities that have been formally notified that they are potentially responsible parties ( PRPs ) under CERCLA for response costs or NRDs, are jointly and severally responsible under the Comprehensive Environmental Response, Compensation and Liability Act ( CERCLA or Superfund ) for those response actions, response costs, and NRDs, all of which may total in excess of $1 billion.

Table of Contents

The PRPs consist of us, Appleton Papers Inc. ( API ), CBC Coating, Inc. (formerly known as Riverside Paper Corporation), Georgia-Pacific Consumer Products, L.P. (formerly known as Fort James Operating Company), Menasha Corporation, NCR Corporation, U.S. Paper Mills Corp., and WTM I.

The Governments have identified manufacturing and recycling of NCR®-brand carbonless copy paper as the principal source of the PCBs in sediments at the Site. Our predecessor, the Bergstrom Paper Company, and later we operated a deinking paper mill in Neenah, Wisconsin, that received NCR®-brand carbonless copy paper in its furnish, and discharged PCBs to Little Lake Butte des Morts, an impoundment of the river at the upstream end of the Site.

The United States Environmental Protection Agency ( EPA ) has divided the lower Fox River and the Bay of Green Bay site into five operable units , including the most upstream ( OU1 ) and four downstream reaches of the river and bay ( OU2-5 ). OU1 extends from primarily Lake Winnebago to the dam at Appleton, and is comprised of Little Lake Butte des Morts. The Neenah Facility discharged its wastewater into this portion of this site.

We have resolved our liability for response actions and response costs associated with the permanent cleanup of Little Lake Butte des Morts through a consent decree, and amendments, entered in *United States v. P.H. Glatfelter Co.*, No. 2:03-cv-949-LA (E.D. Wis.). Together with WTM I Company and with assistance from Menasha Corporation, we have completed that cleanup except for on-going operation and maintenance.

In November 2007, the United States Environmental Protection Agency ( EPA ) issued a unilateral administrative order for remedial action ( UAO ) to us and to seven other respondents directing us to implement the cleanup of the Site downstream of Little Lake Butte des Morts. Since that time, the district court has held that one of the respondents, Appleton Papers Inc., is not liable for this Site. In addition, the United States and the State of Wisconsin have entered into a settlement with another respondent, Georgia-Pacific LLP ( GP ), limiting GP s responsibility to the downstream-most three miles of the river. Work has proceeded to implement the UAO, mostly funded by NCR and its indemnitors.

In January 2008, two of the UAO respondents, NCR Corporation and Appleton Papers Inc., brought two actions consolidated under the caption *Appleton Papers Inc. v. George A. Whiting Paper Co.*, No. 2:08-cv-16-WCG (E.D. Wis.)( Whiting ), that ultimately involved us and more than two dozen parties in litigation to allocate

among the parties the responsibility for response actions, response costs, and NRDs for this Site. Most of the parties responsible for relatively small discharges of PCBs settled with the Governments, resolving their liability. As the result of a series of rulings on summary judgment and after trial, the Court has so far determined that (a) neither NCR nor Appleton Papers may pursue any other party for contribution, (b) NCR owes us and the other non-settling parties full contribution for any amounts we may have to pay on account of response actions or response costs downstream of Little Lake Butte des Morts or NRDs, and (c) NCR is not liable for response costs, response actions, or NRDs in Little Lake Butte des Morts. A single issue remains concerning set off of our insurance coverage litigation settlement proceeds against our recovery from NCR of $4.28 million in costs we incurred in the past. Upon resolution of that issue, we anticipate entry of a final judgment and appeals by NCR and others of those portions of the rulings with which those parties disagree. Until the Whiting Litigation judgment becomes final and is affirmed on appeal, all past and future costs or damages incurred by any person remain the subject of litigation against us.

In October 2010, the United States and the State of Wisconsin sued us and thirteen other defendants to recover an injunction requiring the UAO respondents to complete the response actions required by the UAO and all parties to reimburse past and future response costs incurred by the Governments as well as to pay NRDs. That case is captioned *United States v. NCR Corp.*, No. 1:10-cv-910-WCG (E.D. Wis.) ( Government Action ). To date, litigation of the Government Action has been limited to the United States claim against the UAO respondents for a mandatory injunction to require implementation of the remaining work under the UAO, that is, completion of the remedy in the 33 miles of the river downstream of Little Lake Butte des Morts.

As the result of a series of summary judgment and other rulings, the district court in the Government Action has held that the remedy selected by the Governments and ordered to be implemented by the UAO may be enforced. The district court has further held that all the UAO respondents other than Appleton Papers are jointly and severally liable for the response actions called for by the UAO, unless any of them can establish the defense of divisibility or apportionment. We contend that discharges to Little Lake Butte des Morts did not cause the need for any of the clean up downstream, that the Site is therefore divisible, and that we are therefore not liable for the response actions the United States seeks.

The United States entitlement to injunctive relief, our defense of divisibility (which we share with the other parties responsible for discharges to Little Lake Butte des Morts), and NCR s defense of apportionment were tried to the court in December 2012. Briefing is not yet complete, and the court has yet to rule. The grant or denial of an injunction will be immediately appealable. Other claims will remain to adjudicate after the court rules on the claim for an injunction.

**Cost estimates.** Estimates of the Site remediation change over time as we, or others, gain additional data and experience at the Site. In addition, disagreement exists over the likely costs for some of this work. Based upon estimates made by the Governments and independent estimates commissioned by various potentially responsible parties, we have no reason to disagree with the Governments assertion that total past and future costs and NRDs at this site may exceed $1 billion and that $1.5 billion is a reasonable outside estimate. Much of that amount has already been incurred. As described below, some of that amount is NRDs. The parties implementing the response action under the UAO in the downstream part of the river estimate the future cost of work yet to be done at $360 million.

**NRDs.** The Governments NRD assessment documents claimed that we are jointly and severally responsible for NRDs with a value between $176 million and $333 million. The Governments now claim that this range should be inflated to 2009 dollars and then certain unreimbursed past assessment costs should be added, so that the range of their claim would be $287 million to $423 million. We deny liability for most of these NRDs and believe that even if anyone is liable, that we are not jointly and severally liable for the full amount. Moreover, we believe that the Trustees may not legally pursue this claim at this late date, as the limitations period for NRD claims is three years from discovery.

**Allocation and Divisibility.** We contend that we are not jointly and severally liable for costs or damages arising from the presence of PCBs downstream of Little Lake Butte des Morts. That issue was tried in December 2012. In addition, the district court has ruled that NCR would owe us full contribution for any response actions, response costs, or NRDs that we are ordered to do or to pay in the Government Action.

**Reserves for the Site.** As of December 31, 2012, our reserve for our claimed liability at the Site, including our remediation and ongoing monitoring obligations in Little Lake Butte des Morts, our claimed liability for the remediation of the rest of the Site, our claimed liability for NRDs associated with PCB contamination at the Site and

all pending, threatened or asserted and unasserted claims against us relating to PCB contamination at the Site totaled $16.4 million. Of our total reserve for the Fox River, $0.1 million is recorded in the accompanying condensed consolidated balance sheets under the caption Environmental liabilities and the remainder is recorded under the caption Other long term liabilities.

Although we believe that amounts already funded by us and WTM I to implement the Little Lake Butte des Morts remedy are adequate and no payments have been required since January 2009, there can be no assurance that these amounts will in fact suffice. WTM I has filed a bankruptcy petition in the Bankruptcy Court in Richmond; accordingly, there can be no assurance that WTM I will be able to fulfill its obligation to pay half of any additional costs, if required.

We believe that we have strong defenses to liability for further remediation downstream of Little Lake Butte des Morts, including the existence of ample data that indicate that PCBs did not leave Little Lake Butte des Morts in concentrations that could have caused or contributed to the need for additional cleanup downstream. Others, including the EPA and other parties, disagree with us and, as a result, the EPA has issued a UAO to us and to others to perform the additional remedial work, and filed the Government Action seeking, in part, the same relief. NCR and Appleton Papers commenced the Whiting Litigation and joined us and others as defendants, but, to this point, have not prevailed.

Even if we are not successful in establishing that we have no further remediation liability, we do not believe that we would be allocated a significant percentage share of liability in any equitable allocation of the remediation costs and natural resource damages. The accompanying consolidated financial statements do not include reserves for defense costs for the Whiting Litigation, the Government Action, or any future defense costs related to our involvement at the Site, which could be significant.

In setting our reserve for the Site, we have assessed our legal defenses, including our successful defenses to the allegations made in the Whiting Litigation, and assumed that we will not bear the entire cost of remediation or damages to the exclusion of other known parties at the Site, who are also potentially jointly and severally liable. The existence and ability of other parties to participate has also been taken into account in setting our reserve, and is generally based on our evaluation of recent publicly available financial information on certain of the responsible parties and any known insurance, indemnity or cost sharing agreements between responsible parties and third parties. In addition, our assessment is based upon the magnitude, nature, location and circumstances associated with the various discharges of PCBs to the river and the relationship of those discharges to identified contamination. We will continue to evaluate our exposure and the level of our reserves, including, but not limited to, our potential share of the costs and NRDs, if any, associated with the Site.

The amount and timing of future expenditures for environmental compliance, cleanup, remediation and personal injury, NRDs and property damage liabilities cannot be ascertained with any certainty due to, among other things, the unknown extent and nature of any contamination, the response actions that may ultimately be required, the availability of remediation equipment, and landfill space, and the number and financial resources of any other PRPs.

**Other Information.** The Governments have published studies estimating the amount of PCBs discharged by each identified potentially responsible party s ( PRP s ) facility to the lower Fox River and Green Bay. These reports estimate our Neenah mill s share of the mass of PCBs discharged to be as high as 27%. We do not believe the discharge mass estimates used in these studies are accurate because (a) the studies themselves disclose that they are not accurate and (b) the PCB mass estimates contained in the studies are based on assumptions that are unsupported by existing data on the Site. We believe that the Neenah mill s absolute and relative contribution of PCB mass is significantly lower than the estimates set forth in these studies.

In any event, based upon the rulings in the Whiting Litigation and the Government Action, we continue to believe that an allocation in proportion to mass of PCBs discharged would not constitute an equitable allocation of the potential liability for the contamination at the Fox River. We contend that other factors, such as the location of contamination, the location of discharge, and a party s role in causing discharge, must be considered in order for the allocation to be equitable.

In the 1990s, we entered into interim cost-sharing agreements with six of the other PRPs, which provided for those PRPs to share certain costs relating to scientific studies of PCBs discharged at the Site ( Interim Cost Sharing Agreements ). These Interim Cost Sharing Agreements do not establish the final allocation of remediation costs incurred at the Site. Based upon our evaluation of the rulings in the Whiting Litigation as well as the volume, nature and location of the various discharges of PCBs at the Site and the relationship of those

discharges to identified contamination, we believe our allocable share of liability at the Site is less than our share of costs under the Interim Cost Sharing Agreements.

**Range of Reasonably Possible Outcomes.** Our analysis of the range of reasonably possible outcomes is derived from all available information, including but not limited to official documents such as records of decision, discussions with the United States and other parties, as well as legal counsel and engineering consultants. Based on our analysis of the current records of decision and cost estimates for work to be performed at the Site, we believe that it is reasonably possible that our costs associated with the Fox River matter may exceed our cost estimates and the aggregate amounts accrued for the Fox River matter by amounts that are insignificant or that could range up to $275 million over an undeterminable period that could range beyond 10 years. We believe that the likelihood of an outcome in the upper end of the monetary range is significantly less than other possible outcomes within the range and that the possibility of an outcome in excess of the upper end of the monetary range is remote. The rulings in our favor in the Whiting Litigation, if sustained on appeal, suggest that outcomes in the upper end of the monetary range have become somewhat less likely, while adverse rulings on some issues in the Whiting Litigation and the Government Action and increases in cost estimates for some of the work may make an outcome in the upper end of the range more likely.

**Summary.** Our current assessment is that we will be able to manage this environmental matter without a long-term, material adverse impact on the Company. This matter could, however, at any particular time or for any particular year or years, have a material adverse effect on our consolidated financial position, liquidity and/or results of operations or could result in a default under our debt covenants. Moreover, there can be no assurance that our reserves will be adequate to provide for future obligations related to this matter, that our share of costs and/or damages will not exceed our available resources, or that such obligations will not have a long-term, material adverse effect on our consolidated financial position, liquidity or results of operations. Should a court grant the United States or the State of Wisconsin relief that requires us either to perform directly or to contribute significant amounts towards remedial action downstream of Little Lake Butte des Morts or to NRDs, those developments could have a material adverse effect on our consolidated financial position, liquidity and results of operations and might result in a default under our loan covenants.

**Table of Contents**

### 22. SEGMENT AND GEOGRAPHIC INFORMATION

The following tables set forth profitability and other information by business unit:

For the year ended December 31, 2012

| *In millions* | Specialty Papers | Composite Fibers | Advanced Airlaid Materials | Other and Unallocated | Total |
|---|---|---|---|---|---|
| Net sales | **$ 894.8** | **$ 436.7** | **$ 246.3** | **$** | **$ 1,577.8** |
| Energy and related sales, net | **7.0** | | | | **7.0** |
| Total revenue | **901.8** | **436.7** | **246.3** | | **1,584.8** |
| Cost of products sold | **779.5** | **362.6** | **218.7** | **10.3** | **1,371.1** |
| Gross profit | **122.3** | **74.2** | **27.6** | **(10.4)** | **213.6** |
| SG&A | **55.0** | **38.1** | **9.6** | **18.9** | **121.6** |
| Gains on dispositions of plant, equipment and timberlands, net | | | | **(9.8)** | **(9.8)** |
| Total operating income (loss) | **67.3** | **36.1** | **18.0** | **(19.5)** | **101.9** |
| Non-operating expense | | | | **(22.9)** | **(22.9)** |
| Income (loss) before income taxes | **$ 67.3** | **$ 36.1** | **$ 18.0** | **$ (42.4)** | **$ 78.9** |
| **Supplementary Data** | | | | | |
| Plant, equipment and timberlands, net | **$ 247.9** | **$ 200.1** | **$ 172.9** | **$ 0.3** | **$ 621.2** |
| Depreciation, depletion and amortization | **37.4** | **23.5** | **8.7** | | **69.5** |
| Capital expenditures | **23.1** | **31.4** | **3.9** | **0.3** | **58.8** |

For the year ended December 31, 2011

| *In millions* | Specialty Papers | Composite Fibers | Advanced Airlaid Materials | Other and Unallocated | Total |
|---|---|---|---|---|---|
| Net sales | $ 875.1 | $ 476.0 | $ 252.0 | $ | $ 1,603.2 |
| Energy and related sales, net | 9.3 | | | | 9.3 |
| Total revenue | 884.4 | 476.0 | 252.0 | | 1,612.5 |
| Cost of products sold | 775.7 | 395.7 | 227.7 | 7.2 | 1,406.3 |
| Gross profit | 108.7 | 80.3 | 24.3 | (7.2) | 206.2 |
| SG&A | 51.4 | 39.5 | 10.9 | 23.0 | 124.9 |
| Gains on dispositions of plant, equipment and timberlands, net | | | | (4.0) | (4.0) |
| Total operating income (loss) | 57.3 | 40.8 | 13.4 | (26.2) | 85.3 |
| Non-operating expense | | | | (34.4) | (34.4) |
| Income (loss) before income taxes | $ 57.3 | $ 40.8 | $ 13.4 | (60.7) | $ 50.8 |
| **Supplementary Data** | | | | | |
| Plant, equipment and timberlands, net | $ 250.2 | $ 176.2 | $ 175.6 | $ | $ 602.0 |
| Depreciation, depletion and amortization | 36.0 | 24.8 | 8.5 | | 69.3 |
| Capital expenditures | 31.4 | 22.5 | 10.6 | | 64.5 |

For the year ended December 31, 2010

| *In millions* | Specialty Papers | Composite Fibers | Advanced Airlaid Materials | Other and Unallocated | Total |
|---|---|---|---|---|---|
| Net sales | $ 842.6 | $ 419.2 | $ 193.5 | $ | $ 1,455.3 |
| Energy and related sales, net | 10.7 | | | | 10.7 |
| Total revenue | 853.3 | 419.2 | 193.5 | | 1,466.0 |
| Cost of products sold | 740.2 | 350.5 | 181.7 | 7.4 | 1,279.7 |

| | | | | | |
|---|---|---|---|---|---|
| Gross profit | 113.1 | 68.7 | 11.8 | (7.4) | 186.2 |
| SG&A | 54.7 | 35.8 | 7.4 | 24.3 | 122.1 |
| Gains on dispositions of plant, equipment and timberlands, net | | | | (0.5) | (0.5) |
| Total operating income (loss) | 58.4 | 32.9 | 4.4 | (31.2) | 64.6 |
| Non-operating expense | | | | (31.1) | (31.1) |
| Income (loss) before income taxes | $ 58.4 | $ 32.9 | $ 4.4 | $ (62.3) | $ 33.5 |
| **Supplementary Data** | | | | | |
| Plant, equipment and timberlands, net | $ 251.3 | $ 181.6 | $ 175.3 | $ | $ 608.2 |
| Depreciation, depletion and amortization | 34.9 | 23.7 | 7.2 | | 65.8 |
| Capital expenditures | 24.1 | 8.2 | 4.2 | | 36.5 |

The sum of individual amounts set forth above may not agree to the consolidated financial statements included herein due to rounding.

Table of Contents

Results of individual business units are presented based on our management accounting practices and management structure. There is no comprehensive, authoritative body of guidance for management accounting equivalent to accounting principles generally accepted in the United States of America; therefore, the financial results of individual business units are not necessarily comparable with similar information for any other company. The management accounting process uses assumptions and allocations to measure performance of the business units. Methodologies are refined from time to time as management accounting practices are enhanced and businesses change. The costs incurred by support areas not directly aligned with the business unit are allocated primarily based on an estimated utilization of support area services.

Management evaluates results of operations of the business units before pension income or expense, alternative fuel mixture credits, debt redemption costs, restructuring related charges, certain corporate level costs, and the effects of certain asset dispositions. Management believes that this is a more meaningful representation of the operating performance of its core businesses, the profitability of business units and the extent of cash flow generated from these core operations. Such amounts are presented under the caption Other and Unallocated. This presentation is aligned with the management and operating structure of our company. It is also on this basis that the Company s performance is evaluated internally and by the Company s Board of Directors.

Our Specialty Papers business unit focuses on producing papers for the following markets:

**Carbonless & forms** papers for credit card receipts, multi-part forms, security papers and other end-user applications;

**Book publishing** papers for the production of high quality hardbound books and other book publishing needs;

**Envelope and converting** papers for the direct mail market, shopping bags, and other converting applications; and

**Engineered products** for digital imaging, casting, release, transfer, playing card, postal, FDA-compliant food and beverage applications, and other niche specialty applications.

Specialty Papers revenue composition by market consisted of the following for the years indicated:

| *In thousands* | **2012** | 2011 | 2010 |
|---|---|---|---|
| Carbonless & forms | **$ 372,950** | $ 368,582 | $ 359,033 |
| Book publishing | **155,925** | 166,506 | 168,155 |
| Envelope & converting | **174,781** | 170,380 | 157,202 |
| Engineered products | **187,724** | 166,660 | 155,257 |
| Other | **3,397** | 2,950 | 2,967 |
| Total | **$ 894,777** | $ 875,078 | $ 842,614 |

Our Composite Fibers business unit serves customers globally and focuses on higher value-added products in the following markets:

**Food & Beverage** papers used for single-serve coffee and tea products and other applications;

**Metallized** products used in the labeling of beer bottles, packaging innerliners, gift wrap, self-adhesive labels and other consumer products applications;

**Composite Laminates** papers used in production of decorative laminates, furniture and flooring applications; and

**Technical Specialties** is a diverse line of paper products used in batteries, adhesive tapes and other highly engineered applications.
Composite Fibers revenue composition by market consisted of the following for the years indicated:

| *In thousands* | **2012** | 2011 | 2010 |
|---|---|---|---|
| Food & beverage | **$ 265,423** | $ 284,748 | $ 242,882 |
| Metallized | **87,720** | 95,276 | 88,753 |
| Composite laminates | **44,613** | 53,334 | 50,801 |
| Technical specialties and other | **38,984** | 42,671 | 36,781 |
| Total | **$ 436,740** | $ 476,029 | $ 419,217 |

**Table of Contents**

On February 12, 2010, we acquired Concert Industries Corp., which we now operate as the Advanced Airlaid Materials business unit. This business unit is a leading global supplier of highly absorbent cellulose-based airlaid non-woven materials used to manufacture a diverse range of consumer and industrial products for growing global end-user markets. These products include:

- feminine hygiene;
- adult incontinence;
- home care;
- specialty wipes;
- table top; and
- food pads.

Advanced Airlaid Materials revenue composition by market consisted of the following for the years indicated:

| *In thousands* | **2012** | 2011 | 2010 |
|---|---|---|---|
| Feminine hygiene | **$ 197,792** | $ 206,724 | $ 157,660 |
| Home care | **14,527** | 15,308 | 13,691 |
| Wipes | **13,562** | 5,463 | |
| Adult incontinence | **6,959** | 6,083 | 6,167 |
| Other | **13,442** | 18,469 | 15,981 |
| Total | **$ 246,282** | $ 252,047 | $ 193,499 |

No individual customer accounted for more than 10% of our consolidated net sales in 2012, 2011 or 2010. However, one customer accounted for the majority of Advanced Airlaid Materials net sales in 2012, 2011 and 2010.

Our net sales to external customers and location of net plant, equipment and timberlands are summarized below. Net sales are attributed to countries based upon origin of shipment.

| | **2012** | | 2011 | | 2010 | |
|---|---|---|---|---|---|---|
| *In thousands* | Net sales | Plant, Equipment and Timberlands Net | Net sales | Plant, Equipment and Timberlands Net | Net sales | Plant, Equipment and Timberlands Net |
| United States | **$ 952,195** | **$ 248,185** | $ 933,357 | $ 250,217 | $ 880,089 | $ 251,318 |
| Germany | **358,442** | **191,559** | 410,183 | 181,537 | 327,952 | 198,585 |
| United Kingdom | **119,092** | **59,131** | 122,218 | 57,634 | 128,598 | 55,672 |
| Canada | **106,702** | **83,796** | 88,018 | 86,079 | 75,195 | 80,177 |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Other | **41,357** | | **38,515** | 49,378 | | 26,483 | 43,497 | | 22,418 |
| Total | **$ 1,577,788** | **$** | **621,186** | $ 1,603,154 | $ | 601,950 | $ 1,455,331 | $ | 608,170 |

Table of Contents

**23. GUARANTOR FINANCIAL STATEMENTS**

Our 5.375% Notes are fully and unconditionally guaranteed, on a joint and several basis, by certain of our 100%-owned domestic subsidiaries, PHG Tea Leaves, Inc., Mollanvick, Inc., The Glatfelter Pulp Wood Company, and Glatfelter Holdings, LLC. The guarantees are subject to certain customary release provisions including i) the designation of such subsidiary as an unrestricted or excluded subsidiary; (ii) in connection with any sale or disposition of the capital stock of the subsidiary guarantor; and (iii) upon our exercise of our legal defeasance option or our covenant defeasance option, all of which are more fully described in the Indenture, dated as of October 3, 2012 among us, the Guarantors and U.S. Bank National Association, as Trustee, relating to the 5.375% Notes. The following presents our consolidating statements of income, including comprehensive income, and cash flows for the years ended December 31, 2012, 2011 and 2010 and our consolidating balance sheets as of December 31, 2012 and 2011. These financial statements reflect P. H. Glatfelter Company (the parent), the guarantor subsidiaries (on a combined basis), the non-guarantor subsidiaries (on a combined basis) and elimination entries necessary to combine such entities on a consolidated basis.

**Condensed Consolidating Statement of Income for the**

**year ended December 31, 2012**

| *In thousands* | Parent Company | Guarantors | Non Guarantors | Adjustments/ Eliminations | Consolidated |
|---|---|---|---|---|---|
| Net sales | **$ 894,777** | **$ 53,838** | **$ 683,022** | **$ (53,849)** | **$ 1,577,788** |
| Energy and related sales, net | **7,000** | | | | **7,000** |
| Total revenues | **901,777** | **53,838** | **683,022** | **(53,849)** | **1,584,788** |
| Costs of products sold | **794,364** | **49,061** | **581,544** | **(53,830)** | **1,371,139** |
| Gross profit | **107,413** | **4,777** | **101,478** | **(19)** | **213,649** |
| Selling, general and administrative expenses | **71,228** | **2,818** | **47,544** | | **121,590** |
| Gains on dispositions of plant, equipment and timberlands, net | **(514)** | **(9,276)** | **(25)** | | **(9,815)** |
| Operating income | **36,699** | **11,235** | **53,959** | **(19)** | **101,874** |
| Other non-operating income (expense) | | | | | |
| Interest expense | **(18,689)** | | **(5)** | | **(18,694)** |
| Interest income | **(2,867)** | **6,831** | **(3,504)** | | **460** |
| Other, net | **40,332** | **749** | **1,283** | **(47,063)** | **(4,699)** |
| Total other non-operating income (expense) | **18,776** | **7,580** | **(2,226)** | **(47,063)** | **(22,933)** |
| Income (loss) before income taxes | **55,475** | **18,815** | **51,733** | **(47,082)** | **78,941** |
| Income tax provision | | | | | |
| (benefit) | **(3,904)** | **6,585** | **16,889** | **(8)** | **19,562** |
| Net income (loss) | **59,379** | **12,230** | **34,844** | **(47,074)** | **59,379** |
| Other comprehensive income | **2,775** | **3,243** | **3,920** | **(7,163)** | **2,775** |
| Comprehensive income | **$ 62,154** | **$ 15,473** | **$ 38,764** | **$ (54,237)** | **$ 62,154** |

**Condensed Consolidating Statement of Income for the**

**year ended December 31, 2011**

| *In thousands* | Parent Company | Guarantors | Non Guarantors | Adjustments/ Eliminations | Consolidated |
|---|---|---|---|---|---|
| Net sales | $ 875,077 | $ 50,837 | $ 728,077 | $ (50,837) | $ 1,603,154 |
| Energy and related sales, net | 9,344 | | | | 9,344 |
| Total revenues | 884,421 | 50,837 | 728,077 | (50,837) | 1,612,498 |
| Costs of products sold | 787,216 | 47,330 | 622,841 | (51,082) | 1,406,305 |
| Gross profit | 97,205 | 3,507 | 105,236 | 245 | 206,193 |
| Selling, general and administrative expenses | 70,632 | 2,681 | 51,558 | | 124,871 |
| Gains on dispositions of plant, equipment and timberlands, net | (348) | (3,590) | (12) | | (3,950) |
| Operating income | 26,921 | 4,416 | 53,690 | 245 | 85,272 |
| Other non-operating income (expense) | | | | | |
| Interest expense | (30,741) | | (1,053) | | (31,794) |
| Interest income | 2,706 | 7,838 | (5,578) | (4,300) | 666 |
| Other, net | 41,954 | 467 | 1,447 | (47,167) | (3,299) |
| Total other non-operating income (expense) | 13,919 | 8,305 | (5,184) | (51,467) | (34,427) |
| Income (loss) before income taxes | 40,840 | 12,721 | 48,506 | (51,222) | 50,845 |
| Income tax provision (benefit) | (1,854) | 2,161 | 9,369 | (1,525) | 8,151 |
| Net income (loss) | 42,694 | 10,560 | 39,137 | (49,697) | 42,694 |
| Other comprehensive income | (45,494) | (3,350) | (5,276) | 8,626 | (45,494) |
| Comprehensive income | $ (2,800) | $ 7,210 | $ 33,861 | $ (41,071) | $ (2,800) |

**Condensed Consolidating Statement of Income for the**

**year ended December 31, 2010**

| In thousands | Parent Company | Guarantors | Non Guarantors | Adjustments/ Eliminations | Consolidated |
|---|---|---|---|---|---|
| Net sales | $ 842,615 | $ 49,919 | $ 612,716 | $ (49,919) | $ 1,455,331 |
| Energy and related sales net | 10,653 | | | | 10,653 |
| Total revenues | 853,268 | 49,919 | 612,716 | (49,919) | 1,465,984 |
| Costs of products sold | 753,562 | 43,468 | 532,454 | (49,747) | 1,279,737 |
| Gross profit | 99,706 | 6,451 | 80,262 | (172) | 186,247 |
| Selling, general and administrative expenses | 73,802 | 2,287 | 46,022 | | 122,111 |
| Gains on dispositions of plant, equipment and timberlands, net | (123) | (373) | 43 | | (453) |
| Operating income | 26,027 | 4,537 | 34,197 | (172) | 64,589 |
| Other non-operating income (expense) | | | | | |
| Interest expense | (24,306) | | (1,241) | | (25,547) |
| Interest income | (657) | 7,445 | (4,665) | (1,315) | 808 |
| Other, net | 24,428 | (1,218) | 330 | (29,861) | (6,321) |
| Total other non-operating income (expense) | (535) | 6,227 | (5,576) | (31,176) | (31,060) |
| Income (loss) before income taxes | 25,492 | 10,764 | 28,621 | (31,348) | 33,529 |
| Income tax provision (benefit) | (28,942) | 2,463 | 6,142 | (568) | (20,905) |
| Net income (loss) | 54,434 | 8,301 | 22,479 | (30,708) | 54,434 |
| Other comprehensive income | (1,362) | (6,875) | (15,406) | 22,281 | (1,362) |
| Comprehensive income | $ 53,072 | $ 1,426 | $ 7,073 | $ (8,499) | $ 53,072 |

Table of Contents

**Condensed Consolidating Balance Sheet as of December 31, 2012**

| *In thousands* | Parent Company | Guarantors | Non Guarantors | Adjustments/ Eliminations | Consolidated |
|---|---|---|---|---|---|
| **Assets** | | | | | |
| **Current assets** | | | | | |
| Cash and cash equivalents | **$ 43,748** | **$ 4,311** | **$ 49,620** | **$** | **$ 97,679** |
| Other current assets | **204,961** | **387,627** | **214,568** | **(385,977)** | **421,179** |
| Plant, equipment and timberlands, net | **241,969** | **6,204** | **373,013** | | **621,186** |
| Other assets | **787,348** | **160,741** | **45,133** | **(890,281)** | **102,941** |
| Total assets | **$ 1,278,026** | **$ 558,883** | **$ 682,334** | **$ (1,276,258)** | **$ 1,242,985** |
| **Liabilities and Shareholders Equity** | | | | | |
| Current liabilities | **$ 337,761** | **$ 6,041** | **$ 291,547** | **$ (384,441)** | **$ 250,908** |
| Long-term debt | **250,000** | | | | **250,000** |
| Deferred income taxes | **34,604** | **3,691** | **40,972** | **(17,221)** | **62,046** |
| Other long-term liabilities | **115,982** | **10,602** | **11,093** | **2,675** | **140,352** |
| Total liabilities | **738,347** | **20,334** | **343,612** | **(398,987)** | **703,306** |
| Shareholders equity | **539,679** | **538,549** | **338,722** | **(877,271)** | **539,679** |
| Total liabilities and shareholders equity | **$ 1,278,026** | **$ 558,883** | **$ 682,334** | **$ (1,276,258)** | **$ 1,242,985** |

**Condensed Consolidating Balance Sheet as of December 31, 2011**

| *In thousands* | Parent Company | Guarantors | Non Guarantors | Adjustments/ Eliminations | Consolidated |
|---|---|---|---|---|---|
| **Assets** | | | | | |
| **Current assets** | | | | | |
| Cash and cash equivalents | $ 3,007 | $ 2,894 | $ | | |