

KAPSTONE PAPER & PACKAGING CORP  
Form 10-K  
February 27, 2015

Table of Contents

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

---

**FORM 10-K**

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

**For the fiscal year ended December 31, 2014**

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

**For the transition period from \_\_\_\_\_ to \_\_\_\_\_,  
Commission File No.: 001-33494**

---

**KapStone Paper and Packaging Corporation**

(Exact name of registrant as specified in its charter)

**Delaware**  
(State or other jurisdiction of  
incorporation or organization)

**20-2699372**  
(I.R.S. Employer  
Identification No.)

**KapStone Paper and Packaging Corporation  
1101 Skokie Blvd. Suite 300  
Northbrook, IL 60062**

(Address of principal executive offices) (ZIP Code)

Registrant's telephone number, including area code: **(847) 239-8800**

SECURITIES REGISTERED PURSUANT TO SECTION 12(b) OF THE ACT:

<b>Title of Each Class</b>	<b>Name of Exchange On Which Registered</b>
Common Stock (Par Value \$0.0001)	New York Stock Exchange

SECURITIES REGISTERED PURSUANT TO SECTION 12(g) OF THE ACT: **NONE**

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

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 o No ý

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

## Edgar Filing: KAPSTONE PAPER & PACKAGING CORP - Form 10-K

subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for shorter period that the registrant was required to submit and post such files). Yes  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 the 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 smaller reporting company. See the definition of the above in Rule 12b-2 of the Exchange Act.

Large Accelerated Filer  Accelerated Filer  Non-Accelerated Filer  Smaller Reporting Company

(Do not check if a  
smaller reporting company)

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

The aggregate market value of the 83,731,109 shares of Common Stock held by non-affiliates of the registrant on June 30, 2014, was \$2,774,011,641. This calculation was made using a price per share of Common Stock of \$33.13; the closing price of the Common Stock on the New York Stock Exchange on June 30, 2014 the last day of the registrant's most recently completed second fiscal quarter of 2014. Solely for purposes of this calculation, all shares held by directors and executive officers of the registrant have been excluded. This exclusion should not be deemed an admission that these individuals are affiliates of the registrant.

On February 18, 2015, there were 96,085,557 shares of Common Stock outstanding.

### **DOCUMENTS INCORPORATED BY REFERENCE:**

The registrant's Definitive Proxy Statement for its 2015 Annual Meeting of Stockholders will be filed with the Securities and Exchange Commission no later than 120 days after the end of the fiscal year covered by this Form 10-K pursuant to General Instruction G(3) of the Form 10-K. Information from such Definitive Proxy Statement will be incorporated by reference into Part III.

---

Table of Contents

**INDEX**

**Part I**

	<b>Page</b>
<u>Item 1.</u>	<u>2</u>
<u>Item 1A.</u>	<u>11</u>
<u>Item 1B.</u>	<u>17</u>
<u>Item 2.</u>	<u>18</u>
<u>Item 3.</u>	<u>19</u>
<u>Item 4.</u>	<u>19</u>
<b>Part II</b>	
<u>Item 5.</u>	<u>19</u>
<u>Item 6.</u>	<u>21</u>
<u>Item 7.</u>	<u>22</u>
<u>Item 7A.</u>	<u>34</u>
<u>Item 8.</u>	<u>35</u>
<u>Item 9.</u>	<u>35</u>
<u>Item 9A.</u>	<u>35</u>
<u>Item 9B.</u>	<u>36</u>
<b>Part III</b>	
<u>Item 10.</u>	<u>36</u>
<u>Item 11.</u>	<u>36</u>
<u>Item 12.</u>	<u>36</u>
<u>Item 13.</u>	<u>37</u>
<u>Item 14.</u>	<u>37</u>
<b>Part IV</b>	
<u>Item 15.</u>	<u>37</u>
<u>SIGNATURES</u>	<u>40</u>
<u>INDEX TO FINANCIAL STATEMENTS</u>	<u>F-1</u>

Table of Contents

**PART I**

**Item 1. Business**

**KapStone Acquisition History**

KapStone Paper and Packaging Corporation was formed in Delaware as a special purpose acquisition corporation on April 15, 2005 for the purpose of effecting a merger, capital stock exchange, asset acquisition or other similar business combination with an unidentified operating business in the paper, packaging, forest products, and related industries. Unless the context otherwise requires, references to "KapStone," the "Company," "we," "us" and "our" refer to KapStone Paper and Packaging Corporation and its subsidiaries.

On January 2, 2007, we acquired from International Paper Company substantially all of the assets and assumed certain liabilities of the Kraft Papers Business ("KPB") for \$155.0 million, less \$7.8 million of working capital adjustments. The KPB assets consisted of an unbleached kraft paper manufacturing facility in Roanoke Rapids, North Carolina, Ride Rite® Converting, an inflatable dunnage bag manufacturer located in Fordyce, Arkansas, trade accounts receivable and inventories. We subsequently paid an aggregate of \$53.7 million additional purchase price pursuant to contingent earn-out payments based upon achieving certain EBITDA targets.

On July 1, 2008, we acquired from MeadWestvaco Corporation ("MWV") substantially all of the assets and assumed certain liabilities of the Charleston Kraft Division ("CKD") for \$485.0 million (net of cash acquired of \$10.6 million), less \$8.9 million of working capital adjustments. The CKD assets consisted of an unbleached kraft paper manufacturing facility in North Charleston, South Carolina (including a cogeneration facility), chip mills located in Elgin, Hampton, Andrews and Kinards, South Carolina, a lumber mill located in Summerville, South Carolina, trade accounts receivable and inventories.

On March 31, 2009, we completed the sale of our dunnage bag business to Illinois Tool Works Inc. for \$36.0 million, less \$1.1 million of working capital adjustments. The Company considered the sale an opportunity to reduce its debt and focus on its core business.

On October 31, 2011, we acquired U.S. Corrugated Acquisition Inc. ("USC") pursuant to a merger for \$330.0 million in cash plus \$1.9 million of working capital adjustments. USC owned, at the time of the merger, a recycled containerboard paper mill in Cowpens, South Carolina and fourteen corrugated packaging plants across the Eastern and Midwestern United States.

On July 18, 2013, we acquired 100 percent of the stock of Longview Fibre Paper and Packaging, Inc., ("Longview") for \$1.025 billion plus \$41.5 million of working capital adjustments. Longview is a leading manufacturer of high quality containerboard, kraft papers, and corrugated products. Longview's operations include a paper mill located in Longview, Washington equipped with five paper machines which have the capacity to produce approximately 1.3 million tons of containerboard and kraft paper annually. Longview also owns seven converting facilities located in the Pacific Northwest.

The Company operates in one segment, the integrated manufacture and sale of containerboard, corrugated products, and specialty paper for industrial and consumer markets.

**Future Acquisitions**

In an effort to diversify and/or grow our business we have been, and continue to be, engaged in evaluating a number of potential acquisition opportunities. No assurance can be given that we will consummate additional transactions. The structuring and financing of any future acquisitions may be dependent on the terms and availability of additional financing to us that either replaces or does not conflict with the Company's existing senior secured credit facility.

Table of Contents

**General**

KapStone produces containerboard, corrugated products, and specialty paper. In 2014, we produced 2.7 million tons, of which nearly 80 percent was sold to third party converters or shipped to our corrugated products manufacturing plants based in the United States, and 20 percent of which was sold to foreign based customers. In 2014, our corrugating plants produced and sold about 851 thousand tons or 12.9 billion square feet (BSF) of corrugated products in the U.S. Our net sales in 2014 totaled \$2.3 billion, which was comprised of \$1.5 billion of containerboard and corrugated products and \$0.8 billion of specialty paper.

The Company's business is affected by cyclical industry conditions and general economic conditions in the U.S. and in the countries where we export containerboard and specialty paper. These conditions affect the prices which we are able to charge for our products. Our export sales may also be affected by fluctuations in foreign exchange rates and trade policies and relations.

**Industry Overview**

We compete in the containerboard, corrugated products, and specialty paper markets. We view the specialty paper market as including kraft paper, saturating kraft, and unbleached folding carton board.

**Containerboard**

Containerboard, consisting of linerboard and corrugated medium, is primarily used to manufacture corrugated containers for packaging products. U.S. demand for corrugated containers and containerboard tends to be driven by industrial production of processed foods, nondurable goods and certain durable goods.

The American Forest and Paper Association's ("AF&PA") estimate of the size of the U.S. containerboard market is as follows:

<b>(In millions)</b>	<b>2014</b>	<b>2013</b>	<b>2012</b>
Total U.S. sales	31.7 tons	30.8 tons	30.7 tons
U.S. production	35.4 tons	34.8 tons	34.4 tons
Imports	1.0 tons	0.8 tons	0.6 tons
Exports	4.7 tons	4.2 tons	4.3 tons
U.S. operating rates	96%	96%	95%

The primary markets for our containerboard are our corrugated products manufacturing plants and independent corrugated and laminated products customers who focus on specialty niche packaging.

**Corrugated Products**

According to the Fibre Box Association's most recent annual report dated April 2014, the value of industry shipments of corrugated products was \$28.4 billion, an increase of \$2.0 billion, or 7.0 percent.

The primary end-use markets for corrugated products are shown below (as reported in the most recent Fibre Box Association annual report dated April 2014):

Food, beverages and agricultural products	40%
General retail and wholesale trade	21%
Paper products	17%
Miscellaneous manufacturing	12%
Petroleum, plastic, synthetic, and rubber products	7%
Appliances, vehicles, and metal products	3%

Table of Contents

Corrugated products manufacturing plants tend to be located in close proximity to customers to minimize freight costs and shipping times. The Fibre Box Association estimates that the U.S. corrugated products industry consists of approximately 570 companies and over 1,200 plants.

**Specialty Paper**

**Kraft Paper**

We produce three general categories of kraft paper:

**Multiwall paper** is used to produce bags for agricultural products, pet food, baking products, cement and chemicals. We are the only U.S. manufacturer of extensible, high performance multiwall kraft paper. Our FibreShield® and TEA-Kraft® lines of products offer durability, savings, efficiency and are supported by our exceptional customer and technical service. We also manufacture durable flat multiwall sack paper for a variety of end-use applications.

**Specialty products** has a large variety of uses within coating and laminating applications that requires a smooth surface. Specialty products are also used to produce shingle wrap, end caps, roll wrap and dunnage bags. Our specialty paper products are designed to meet the unique needs of a variety of customers and end uses. We modify a range of specialty paper products for our specialty paper grades, such as sizing, smoothness, porosity, wet strength, pH and others. Our specialty paper products are manufactured for a variety of converters, including laminators, coaters, insulation manufacturers, agricultural product processors and food product packaging producers.

**Lightweight paper** is used in a variety of flexible packaging applications that range from 100 percent recycled content for quick-service restaurants carry out bags to 100 percent virgin content for direct contact food packaging. Our lightweight virgin furnished papers are produced from specifically blended wood chip recipes. These wood chip and pulp recipes are specifically designed to develop paper properties important for a variety of specialty packaging end uses and coating base paper applications. Our recycled content light weight papers are made in a wide variety of basis weights and percentages of recycled fiber content, and are valued for their cleanliness, strength, sustainability and end-use possibilities. The most recently developed product line, FibreGreen®, is composed of old corrugated containers ("OCC") processed in our state-of-the-art OCC facility and are available in a wide range of basis weights. FibreGreen® meets the U.S. Food and Drug Administration's requirements for direct food contact and is certified by the Sustainable Forestry Initiative®.

The AF&PA's estimate of the size of the U.S. kraft paper market is as follows:

(In millions)	2014	2013	2012
Total U.S. sales	1.40 tons	1.34 tons	1.34 tons
U.S. production	1.34 tons	1.27 tons	1.28 tons
Imports	0.17 tons	0.18 tons	0.16 tons
Exports	0.21 tons	0.21 tons	0.22 tons
U.S. operating rates	90%	77%	76%

Over the last two decades, unbleached kraft paper production capacity has declined. This decline was primarily driven by plastic bags replacing paper at most grocery stores across North America. The multiwall shipping sack market also contributed to the decrease in capacity resulting from conversion to plastic and woven poly in certain end-use markets, primarily pet food, chemicals and seed and feed markets.

Table of Contents

***Saturating Kraft***

Saturating kraft is used in multiple industries around the world, including construction, electronics manufacturing and furniture manufacturing. The major end-use is thin high pressure laminates (HPL), used to create decorative surfaces such as kitchen and bath countertops, home and office furniture and flooring. Within the HPL market there is a growing and distinct HPL segment manufacturing and selling a much thicker product called compact laminates used as surfacing products such as exterior cladding, partitions and doors. In Asia, there is significant use of saturating kraft product for the manufacturing of printed circuit boards (PCB) and copper clad laminates (CCL) and there is also a growing use for thin HPL in decorative surfaces. We are not aware of any published data reporting the size of the saturating kraft market. Barriers to entry for producing high quality saturating kraft are high as it is a technically difficult grade of paper to produce.

***Unbleached Folding Carton Board***

Unbleached folding carton board is a low density virgin fiber board. Applications are widely spread throughout end uses in the general folding carton segment of the paperboard packaging market. This product can replace the use of more expensive coated recycled board, coated natural kraft board and solid bleached sulfate board which are currently much larger markets. There is no published data we are aware of reporting the size of the unbleached, uncoated folding carton market.

**Manufacturing**

We operate four paper mills, three in the Southeastern region and one in the Pacific Northwest region of the United States. In 2014, we produced 2.7 million tons of containerboard and specialty paper at our mills in North Charleston, South Carolina; Roanoke Rapids, North Carolina; Cowpens, South Carolina and Longview, Washington. Our mills generally operate 24 hours a day, seven days a week. Fiber used to make containerboard and specialty paper is produced from a combination of locally sourced roundwood and woodchips. After the wood is debarked and chipped, the chips are loaded into digesters for cooking. Woodchips, chemicals and steam are mixed in the digester to produce softwood pulp. Hardwood pulp is produced in North Charleston in a similar fashion for the production of DuraSorb® saturating kraft. The pulp is screened and washed through a series of washers, and then stored prior to the paper making process. OCC is used to make recycled containerboard at our Cowpens mill and is a component of certain grades of kraft paper and containerboard at our Longview mill. The Company processes pulp using eleven paper machines at our facilities. Management monitors productivity on a real-time basis with on-line reporting tools that track production values versus targets. Overall equipment efficiency is also monitored daily through production reporting systems.

As of December 31, 2014, we operated 21 corrugated products manufacturing plants, comprised of twelve box plants, seven sheet plants and two sheet feeder plants. Box plants operate as combining operations that manufacture corrugated sheets and finished corrugated products. Sheet feeder plants have a corrugator machine and manufacture corrugated sheets which are shipped to sheet or box plants. Sheet plants have various machines which convert corrugated sheets, purchased either from our operations or third parties, into finished corrugated products. Plants with a corrugating machine have total capacity of approximately eighteen billion square feet ("BSF").

Our corrugated products manufacturing plants operate in fourteen states in the U.S., with no manufacturing facilities outside of the continental U.S. Each plant, for the most part, serves a market radius that typically averages 200 miles. Our sheet plants are generally located in close proximity to our larger corrugated plants, which enables us to offer additional services and converting capabilities, such as small volume and quick turnaround items.

Table of Contents

We produce a wide variety of products ranging from basic corrugated shipping containers to specialized packaging. We also have multi-color printing capabilities to make high-impact graphics boxes and displays that offer customers such as consumer products companies more attractive packaging.

We have dedicated personnel who coordinate and execute all containerboard buy/sell arrangements with other containerboard manufacturers. As is industry practice, we also "trade" among industry participants who are located more closely to converting plants in order to reduce freight costs.

**Distribution**

Containerboard and specialty paper produced in our mills is shipped by rail or truck to customers in the U.S. and is shipped by truck to nearby ports and then by ocean vessel to our export customers. Domestic rail shipments represent about 40 percent of the tons shipped and the remaining 60 percent is shipped by truck.

Our corrugated products are delivered by truck due to our customers demand for timely service. We use a combination of a dedicated third-party fleet and our own trucks.

**Sales and Marketing**

Our containerboard and specialty paper marketing strategy is to sell our products to third-party converters and manufacturers of industrial and consumer packaging products. We seek to meet the quality and service needs of the customers of our corrugated operations at the most efficient cost, while balancing those needs against the demands of our containerboard customers.

We sell our products directly to end users and converters, as well as through sales agents. Our sales groups are responsible for the sale of these products to third party converters in the U.S. Sales to export markets are managed by separate teams of which certain personnel are based in Europe and Asia.

Our corrugated products are sold through an internal sales and marketing organization. We have sales representatives and sales managers who serve local and regional accounts. We also have corporate account managers who serve large national accounts at multiple customer locations. Our corrugated operations focus on supplying both high-volume commodity products and specialized packaging with high-value graphics.

**Customers and Products**

The following represents the Company's sales by product line:

Product Line Revenue:	Years Ended December 31,							
	Net Sales (in thousands)				Tons Sold			
	2014	2013	Increase/ (Decrease)	%	2014	2013	Increase/ (Decrease)	%
Containerboard / Corrugated products	\$ 1,463,670	\$ 1,108,545	\$ 355,125	32.0%	1,764,628	1,403,797	360,831	25.7%
Specialty paper	741,601	551,931	189,670	34.4%	1,031,024	799,261	231,763	29.0%
Other	95,649	87,686	7,963	9.1%				
Product sold	\$ 2,300,920	\$ 1,748,162	\$ 552,758	31.6%	2,795,652	2,203,058	592,594	26.9%

KapStone has over 3,000 U.S.-based and over 200 export customers.

Containerboard is sold to domestic and foreign converters in the corrugated packaging industry and to other converters for a variety of uses including laminated tier sheets and wrapping material,





Table of Contents

among others. Historically, our focus is on independent converters who do not have their own mill systems or converters who otherwise commonly purchase containerboard in the open market.

Corrugated products are sold primarily to regional and local accounts, which are broadly diversified across industries and geographic locations. We have a select number of national accounts, or those customers with a national presence. These national customers typically purchase corrugated products from several of our box plants throughout the United States.

Specialty paper is sold to both domestic and export converters who produce multiwall bags for food grade agricultural products, pet food, cement and chemicals, grocery bags and specialty conversion products, such as wrapping paper products, dunnage bags and roll wrap.

Our saturating kraft paper, sold under the trade name Durasorb®, has a customer base which is split among three geographic regions the Americas, Europe and Asia. Approximately 86 percent of our sales are exports to customers in Europe, Latin America and Asia where growth opportunities are favorable. KapStone, or its predecessor, has done business with many of these customers for well over 40 years. Some customers have consolidated to form a greater presence in their end-use markets. Customer consolidation is particularly evident in North America and is in the early phase in Europe. In Asia, there are numerous players and it is a highly fragmented market making entry difficult for some companies that do not have a presence in the region. KapStone has acquired a leadership position with our Durasorb® product through knowledge of our markets and understanding the technical needs of our customers' manufacturing processes and the demanding requirements of their products.

Our unbleached folding carton board sold under the Kraftpak® trade name has a customer base which consists primarily of integrated and independent converters in the folding carton industry. Our unbleached folding carton board product is a unique, low-density virgin fiber board. KapStone believes that the best growth opportunities for Kraftpak® are in consumer brands that are changing their images to promote environmental friendliness and sustainability. Kraftpak® and similar products replace the use of coated recycled board, coated natural kraft board and solid bleached sulfate board, which are currently much larger markets.

No customer accounts for more than 10 percent of consolidated net sales. Our business is not dependent upon a single customer or upon a small number of major customers. We do not believe the loss of any one customer would have a material adverse effect on our business.

**Seasonality and Backlog**

Demand for our major product lines is relatively constant throughout the year, and seasonal fluctuations in marketing, production, shipments and inventories are not significant. Slight seasonal fluctuations are largely driven by the agricultural market within the western United States. Backlogs are a factor in the industry, as they allow paper mills to run more efficiently. However, most orders are placed for delivery within 30 days.

**Major Raw Materials Used**

Fiber is the single largest cost in the manufacture of containerboard and specialty paper. KapStone consumes both wood fiber and recycled fiber in its paper mills. Our mills in North Charleston and Roanoke Rapids use primarily virgin fiber. The fiber needs in 2014 of our Longview, Washington mill were supplied by approximately 68 percent of virgin fiber and 32 percent recycled fiber. Fiber used to make containerboard and specialty paper is produced from a combination of locally sourced roundwood and woodchips. We rely on supply agreements and open-market purchases to supply these mills with roundwood and wood chips. Fiber resources are generally available within economic proximity to these mills and we have not experienced any significant difficulty in obtaining our mill fiber needs.

Table of Contents

Our mill in Cowpens, South Carolina is a 100 percent recycled mill, whose fiber consumption consists solely of recycled fiber or OCC. We obtain OCC pursuant to certain supply agreements and in open market purchases from suppliers within economic proximity to the Cowpens Mill. OCC has historically exhibited significant price volatility. The Cowpens mill has not experienced any significant difficulty in obtaining OCC.

Our corrugated manufacturing plants consume containerboard produced at our mills or from third parties and through buy/sell arrangements. We use third-party mills which are closer to our corrugated manufacturing plants to realize freight savings. Containerboard, which includes both linerboard and corrugating medium, is the principal raw material used to manufacture corrugated products. Linerboard is used as the inner and outer facings, or liners, of corrugated products. Corrugating medium is fluted and laminated to linerboard in corrugated plants to produce corrugated sheets. The sheets are subsequently printed, cut, folded and glued to produce corrugated products.

**Energy**

Energy at the mills is obtained through purchased electricity or through various fuels, which are converted to steam or electricity on-site. Fuel sources include coal, natural gas, oil, bark, and by-products of the manufacturing and pulping process, including black liquor. These fuels are burned in boilers to produce steam. Steam turbine generators are used to produce electricity. To reduce our mill energy cost, we have invested in processes and equipment to ensure a high level of purchased fuel flexibility. In recent history, fuel oil has exhibited higher costs per thermal unit and more price volatility than natural gas and coal. During 2014, approximately 65 percent of our North Charleston, South Carolina and Roanoke Rapids, North Carolina mills purchased fuel needs were from coal, historically our lowest cost purchased fuel. A substantial portion of our Longview mill electricity requirements are satisfied by hydroelectric power, which has relatively stable pricing.

In 2014, we purchased coal under two contracts that ended on December 31, 2014. In 2015, the Company has one coal contract for all of its needs with contracted pricing through December 31, 2015.

KapStone's corrugated product manufacturing plants primarily use boilers that produce steam which are used to power the corrugating machines. The majority of these boilers burn natural gas, although some also have the ability to burn fuel oil. Sheet plants use electricity for their main source of power.

**Competition**

The markets in which we sell our products are highly competitive and comprised of many participants. We face significant competitors, including large, vertically integrated companies and numerous smaller companies.

Our principal competitors with respect to sales of our containerboard and specialty paper are a number of large, diversified paper companies, including International Paper Company, Georgia-Pacific (owned by Koch Industries, Inc.), Rock-Tenn Company and Packaging Corporation of America, all of which have greater financial resources than we do. We also compete with other regional manufacturers of these products. Our specialty paper products (other than our Durasorb® and Kraftpak® products) are each generally considered a commodity-type product that can be purchased from numerous suppliers and competition is based primarily on price, product specification, service and quality.

Corrugated products businesses seek to differentiate themselves through pricing, quality, service and product design and innovation. We compete for both local and national account business, and we compete against producers of other types of packaging products. On a national level, our primary competitors include International Paper Company, Georgia-Pacific (owned by Koch Industries, Inc.), Rock-Tenn Company and Packaging Corporation of America. However, with our strategic focus on local and regional accounts, we also compete with the smaller independent converters.

Table of Contents

**Intellectual Property**

The Company owns patents, licenses, trademarks and trade names on products. However, we do not believe that our intellectual property is material to our business and the loss of any or our intellectual property rights would not have a material adverse effect on our operations or financial condition.

**Employees**

As of December 31, 2014, we had 4,628 employees. Of these, 1,380 employees are salaried and 3,248 are hourly. Approximately 2,500 of our hourly employees are represented by unions. The majority of our unionized employees are represented by the United Steel Workers (USW).

Currently, there is a collective bargaining agreement in place with trade union employees at our mills in North Charleston through June 2015 and Roanoke Rapids through August 2016. The Company is engaged in negotiations with its union employees in Longview. The mill is operating under the terms of a contract that expired in June 2014. We expect to begin negotiations to renew the North Charleston union contract in early 2015.

We did not experience any work stoppages in 2014 and have not experienced any work stoppages in the eight years prior to 2014. We believe we have good relations with our employees.

**Environmental Matters**

Compliance with environmental requirements is a significant factor in our business operations. We commit substantial resources to maintaining environmental compliance and managing environmental risk. We are subject to, and must comply with, a variety of federal, state and local environmental laws, particularly those relating to air and water quality, waste disposal, and cleanup of contaminated soil, groundwater or rivers. The most significant of these laws affecting us are:

1. Resource Conservation and Recovery Act (RCRA);
2. Clean Water Act (CWA);
3. Clean Air Act (CAA);
4. The Emergency Planning and Community Right-to-Know-Act (EPCRA);
5. Toxic Substance Control Act (TSCA); and
6. Safe Drinking Water Act (SDWA).

We believe that we are currently in material compliance with these and all applicable environmental rules and regulations. Because environmental regulations are constantly evolving, we have incurred, and will continue to incur, costs to maintain compliance with these and other environmental laws and regulations. We work diligently to anticipate and budget for the impact of applicable environmental regulations, and do not currently expect that future environmental compliance obligations will materially affect our business or financial condition.

We do not believe that any ongoing remedial projects are material in nature.

The Company's subsidiary, Longview is a potentially responsible party under the Comprehensive Environmental Response, Compensation and Liability Act ("CERCLA") with respect to the Lower Duwamish Waterway Superfund Site in the State of Washington (the "Site"). The U.S. Environmental Protection Agency ("EPA") asserts that the Site is contaminated as a result of discharges from various businesses and government entities located along the Lower Duwamish Waterway, including a corrugated converting plant owned and operated by Longview. In November 2014, the EPA issued a Record of Decision ("ROD") for the Site. The ROD includes a selected remedy for the Site. In the ROD, EPA states that the total estimated net present value costs (discounted at 2.3%) for the selected



Table of Contents

remedy are \$342 million. At least 40 potentially responsible parties, including Longview, have entered into an Allocation Agreement. Pursuant to the Allocation Agreement, the parties will attempt to determine each party's portion of the cost to remediate the site. The allocation process is not expected to be completed until 2017. Based on available information provided to the Company to date, the Company cannot reasonably estimate its potential liability. We also maintain insurance that may limit our financial exposure for defense costs, as well as liability, if any, for claims covered by the insurance (subject also to deductibles, self-insurance amounts, and retrospective premiums).

We could also incur environmental liabilities as a result of claims by third parties for civil damages, including liability for personal injury or property damage, arising from releases of hazardous substances or contamination. We are not aware of any material claims of this type currently pending against us.

While legislation regarding the regulation of greenhouse gas emissions has been proposed from time to time at the federal level, it is uncertain whether such legislation will be passed and, if so, what the breadth and scope of such legislation will be. The EPA has begun to propose and / or adopt regulations regulating certain aspects of greenhouse gas emissions. To the extent such regulations become applicable to our operations, they could potentially adversely affect the Company. The result of a broader regulation of greenhouse gas emissions could be an increase in our future environmental compliance costs, through caps, taxes or additional capital expenditures to modify facilities, which may be material. However, climate change legislation and the resulting future energy policy could also provide us with opportunities if the use of renewable energy is encouraged. We currently generate a significant portion of our power requirements for our mills using bark, black liquor and biomass as fuel, which are derived from renewable resources. While we believe we are well-positioned to take advantage of any renewable energy incentives, it is uncertain what the ultimate costs and opportunities of any climate change legislation or regulation will be and how our business and industry will be affected.

In 2004, EPA published the Boiler MACT regulations, establishing air emissions standards and certain other requirements for industrial boilers. These regulations have been subject to a series of legal challenges and have been repurposed and / or amended by EPA several times since the initial rules were published. A final reconsidered regulation was issued in January 2013 but legal challenges have been filed and it remains uncertain as to whether the rule as currently promulgated will be further revised. Based upon the Company's current understandings of the rules, it is unclear what the total cost of compliance will be, if any.

In addition to Boiler MACT and greenhouse gas standards, the EPA has recently finalized a number of other environmental rules, which may impact the pulp and paper industry. The EPA also is revising existing environmental standards and developing several new rules that may apply to the industry in the future. We cannot currently predict with certainty how any future changes in environmental laws and regulations (or their interpretation) and/or enforcement practices will affect our business; however, it is possible that our compliance, capital expenditure requirements and operating costs could increase materially.

**Available Information**

We make available free of charge our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports filed or furnished as required by Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended, through our Internet Website ([www.kapstonepaper.com](http://www.kapstonepaper.com)) as soon as is reasonably practicable after we electronically file such material with, or furnish it to, the Securities and Exchange Commission. Information contained in or incorporated into our Internet Website is not incorporated by reference herein.

**Financial Information About Segments and Geographic Areas**

We operate as one segment and our revenues are generated primarily in one geographic region. See "Segment Information" of Note 2 Summary of Significant Accounting Policies and Note 15 Segment Information contained in the "Notes to Consolidated Financial Statements."

Table of Contents

**Item 1A. Risk Factors**

Some of the statements in this report and, in particular, statements found in Management's Discussion and Analysis of Financial Condition and Results of Operations, that are not historical in nature are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements include statements about our expectations regarding our future liquidity, earnings, expenditures and financial condition. These statements are often identified by the words "will," "should," "anticipate," "believe," "expect," "intend," "estimate," "hope," or similar expressions. These statements reflect management's current views with respect to future events and are subject to risks and uncertainties. There are important factors that could cause actual results to differ materially from those in forward-looking statements, many of which are beyond our control. These factors, risks and uncertainties include, but are not limited to, the factors described below.

Our actual results, performance or achievement could differ materially from those expressed in, or implied by, these forward-looking statements, and, accordingly, we can give no assurances that any of the events anticipated by the forward-looking statements will transpire or occur, or if any of them do so, what impact they will have on our results of operations or financial condition. In view of these uncertainties, investors are cautioned not to place undue reliance on these forward-looking statements. We expressly disclaim any obligation to publicly revise any forward looking statements that have been made to reflect the occurrence of events after the date hereof.

**Risks associated with our business**

***We rely on key customers and a loss of one or more of our key customers could adversely affect our business, results of operations, cash flows and financial position.***

During the year ended December 31, 2014, no customer accounted for more than 10 percent of consolidated net sales. However, losses of key customers could significantly impact our business, results of operations, cash flows and financial position.

***We are dependent upon key management executives the loss of whom may adversely impact our business.***

We depend on the expertise, experience and continued services of corporate and mill management. The loss of such management, or an inability to attract or retain other key individuals, could materially adversely affect our business. There can be no assurance that our salaries and incentive compensation plans will allow us to retain the services of these key management executives or hire new key employees.

***Our indebtedness may adversely affect our financial health.***

As of December 31, 2014, we had approximately \$1.1 billion of outstanding debt. As a result of the indebtedness, our ability to obtain additional financing for working capital, capital expenditures, acquisitions or other general corporate purposes may be impaired in the future. The debt could make us vulnerable to economic downturns and may hinder our ability to adjust to rapidly changing market conditions.

A significant portion of our cash flow from operations will be needed to meet the payment of principal and interest on our indebtedness. The business may not generate sufficient cash flow from operations to enable it to repay our indebtedness and to fund other liquidity needs, including capital expenditure requirements. The indebtedness incurred by us under our senior secured credit facility (the "Credit Facility") under our Amended and Restated Credit Agreement bears interest at variable rates, and therefore if interest rates increase, our debt service requirements would increase. In such case, we may need to refinance or restructure all or a portion of our indebtedness on or before maturity. We may not be able to refinance any of our indebtedness, including the Credit Facility, on commercially

Table of Contents

reasonable terms, or at all. If we cannot service or refinance our indebtedness, we may have to take actions such as selling assets, seeking additional equity or reducing or delaying capital expenditures, any of which could have a material adverse effect on our operations and financial condition.

Our Credit Facility contains restrictive covenants that limit our liquidity and corporate activities, including our ability to pursue additional acquisitions. Our Credit Facility imposes operating and financial restrictions that limit our ability to:

incur additional indebtedness;

create additional liens on our assets;

make investments;

engage in mergers or acquisitions;

pay dividends; and

sell all or any substantial part of our assets.

In addition, our Credit Facility also imposes other restrictions on us. Therefore, we would need to seek permission from the lenders in order to engage in certain corporate actions. The lenders' interests may be different from ours, and no assurance can be given that we will be able to obtain the lenders' permission when needed. This may prevent us from taking actions that are in our best interest.

Our Credit Facility requires us to maintain certain financial ratios. The failure to maintain the specified ratios could result in an event of default if not cured or waived.

In the event of a default under our Amended and Restated Credit Agreement, the lenders generally would be able to declare all outstanding indebtedness, together with accrued interest, to be due and payable. In addition, borrowings under the Credit Facility are secured by a first priority lien on substantially all of our assets and, in the event of a default under that facility, the lenders generally would be entitled to seize the collateral. A default under any debt instrument, unless cured or waived, would likely have a material adverse effect on our business, liquidity and financial condition.

***If we fail to extend or renegotiate the collective bargaining agreements as they expire from time to time, or if our unionized employees were to engage in a strike or other work stoppage, our business and operating results could be materially harmed.***

Most of our hourly paid employees are represented by trade unions. We are a party to collective bargaining contracts which apply to approximately 875 employees at various corrugating manufacturing plants, 700 employees at the Longview mill, 560 employees at the North Charleston mill, and 365 employees at the Roanoke Rapids mill. No assurance can be given that we will be able to successfully extend or renegotiate the collective bargaining agreements as they expire from time to time. Currently, there is a collective bargaining agreement in effect with respect to North Charleston through June 2015 and Roanoke Rapids through August 2016. The Longview union contract expired in June 2014 and remains under negotiations. If we are unable to extend or negotiate new agreements without work stoppages, it could negatively impact our ability to manufacture our products and adversely affect our results of operations.



Table of Contents

***We sell some of our products internationally, and, accordingly, our business, results of operations, cash flows and financial position could be adversely affected by the political and economic conditions of the countries in which we conduct business, by fluctuations in exchange rates and other factors related to our international operations.***

Approximately 20 percent of our revenues in 2014 and 2013 were derived from export sales. Our international operations and activities face increasing exposure to the risks of selling to customers in foreign countries. These factors include:

Changes in foreign currency exchange rates which could adversely affect selling prices for our products, and therefore our competitive position in a particular market.

Trade protection measures in favor of local producers of competing products, including government subsidies, tax benefits, trade actions (such as anti-dumping proceedings) and other measures giving local producers a competitive advantage over us.

Changes generally in political, regulatory or economic conditions in the countries in which we sell our products.

These risks could affect the cost of selling our products, our pricing, sales volume, and ultimately our financial performance. The likelihood of such occurrences and their potential effect on the Company vary from country to country and are unpredictable.

***We may be required to record a charge to our earnings if our goodwill becomes impaired.***

We test for impairment of goodwill annually in accordance with generally accepted accounting standards. When events or changes in circumstances indicate that the carrying value for such assets may not be recoverable, we review goodwill for impairment on an interim basis. Factors that may be considered a change in circumstances requiring our interim testing include a decline in stock price as compared to our book value per share, future cash flows and slower growth rates. In connection with future annual or interim tests, we may be required to record a non-cash charge to earnings during the period in which any impairment of goodwill is determined, which would adversely impact our results of operations.

See Note 2, "Significant Accounting Policies - Goodwill and Intangible Assets" in the Notes to the Consolidated Financial Statements for additional information related to testing for impairment of goodwill.

***Our business depends on effective information management systems.***

We rely on our enterprise resource planning (ERP) systems to support such critical business operations as processing sales orders and invoicing, inventory control, purchasing and supply chain management, payroll and human resources and financial reporting. We periodically implement upgrades to such systems or migrate one or more of our affiliates, facilities or operations from one system to another. If we are unable to adequately maintain such systems to support our developing business requirements or effectively manage any upgrade or migration, we could encounter difficulties that could have a material adverse impact on our business, internal controls over financial reporting, financial results or our ability to timely and accurately report such results.

***We are subject to cyber-security risks related to certain customer, employee, vendor or other company data.***

We use information technologies to securely manage operations and various business functions. We rely upon various technologies to process, store and report on our business and interact with customers, vendors and employees. Despite our security design and controls, and those of our third-party providers, we could become subject to cyber attacks which could result in operational disruptions or the

Table of Contents

misappropriation of sensitive data. There can be no assurance that such disruptions or misappropriations and the resulting repercussions will not be material to our results of operations, financial condition or cash flows.

***We may incur business disruptions.***

We take measures to minimize the risks of disruptions at our manufacturing facilities. However, the occurrence of a natural disaster, such as a hurricane, tropical storm, earthquake, tornado, flood, fire or other unanticipated problems, such as labor difficulties, equipment failure or unscheduled maintenance, could cause operational disruptions and could materially adversely affect our earnings and cash flows. Any losses due to these events may not be covered by our existing insurance policies or may be subject to certain deductibles.

***Environmental regulations could materially adversely affect our results of operations and financial position and require us to make unexpected capital expenditures.***

We are subject to environmental regulation by federal, state and local authorities in the United States, including requirements that regulate discharge into the environment, waste management and remediation of environmental contamination. Maintaining compliance with existing and new environmental laws may require material additional capital expenditures.

Due to past history of industrial operations at the Roanoke Rapids mill, North Charleston mill, Longview mill and some of our corrugating manufacturing plants, the possibility of on-site and off-site environmental impact to the soil and groundwater may present a heightened risk of contamination. If we are required to make significant expenditures for remediation, the costs of such efforts may have a significant negative impact on our results of operations, cash flows and financial position.

***Our operations are dependent upon certain operating agreements for fiber.***

We rely on certain supply arrangements to provide us roundwood and woodchips. If one of these suppliers failed to deliver quality roundwood or woodchips in the quantities we require, KapStone's supply may not be adequate to cover customer needs, which could have an adverse effect on our results of operations, cash flows and financial position.

***Our pension costs are subject to a variety of factors and assumptions that could cause these costs to change.***

We have a defined benefit pension plan that covers 54 percent of our employees. Our pension costs are dependent upon a variety of factors and assumptions based upon past experience. Fluctuations in market returns, interest rates, mortality rates, the number of retirees and longer life-expectancy may result in increased pension costs. Similarly, changes in assumptions regarding current discount rates and expected rates of return on plan assets could also change pension costs. Material adverse changes in these factors could have a negative impact on our results of operations, cash flows, and financial position.

**Risks Associated with KapStone's Common Stock**

***The market price for our common stock may be highly volatile.***

The market price of our common stock may be volatile due to certain factors, including, but not limited to: quarterly fluctuations in our financial and operating results; general conditions in the paper and packaging industries; or changes in earnings estimates.

Table of Contents

***Our executive officers and directors control a substantial percentage, approximately 11 percent, of our common stock and thus may influence certain actions requiring a stockholder vote.***

At December 31, 2014, our named executive officers and directors owned 11.0 million shares of our common stock, or approximately 11 percent of our total outstanding common stock. Accordingly, our named executive officers and directors may have some influence over the outcome of all matters requiring approval by our stockholders, including future acquisitions and the election of directors. In addition, our board of directors is divided into three classes, each of which will generally serve for a term of three years with only one class of directors being elected in each year. At the annual meeting, as a consequence of our "staggered" board of directors, only a minority of the board of directors will be considered for election and our officers and directors, because of their ownership position, will have some influence regarding the outcome of the election.

**Risks associated with the paper, packaging, forest products and related industries**

***The paper, packaging, forest products and related industries are highly cyclical. Fluctuations in the prices of and the demand for products could result in smaller profit margins and lower sales volumes.***

Historically, economic and market shifts, fluctuations in capacity and changes in foreign currency exchange rates have created cyclical changes in prices, sales volume and margins for products in the paper, packaging, forest products and related industries. The length and magnitude of industry cycles have varied over time and by product, but generally reflect changes in macroeconomic conditions and levels of industry capacity. Most paper products and many wood products used in the packaging industry are commodities that are widely available from many producers. Because commodity products have few distinguishing qualities from producer to producer, competition for these products is based primarily on price, which is determined by supply relative to demand. The overall levels of demand for these commodity products reflect fluctuations in levels of end-user demand, which depend in large part on general macroeconomic conditions in North America and regional economic conditions in our markets (including Europe, Asia, and Central and South America), as well as foreign currency exchange rates. The foregoing factors could materially and adversely impact our sales, cash flows, profitability and results of operations.

***An increase in the cost or a reduction in the availability of wood fiber, other raw materials, energy and transportation may have an adverse effect on our profitability and results of operations.***

Wood fiber (including OCC) is the principal raw material in many parts of the paper and packaging industry. Wood fiber is a commodity, and prices historically have been cyclical and have varied on a regional basis. Environmental litigation and regulatory developments have caused, and may cause in the future, significant reductions in the amount of timber available for commercial harvest in the United States. In addition, future domestic or foreign legislation and litigation concerning the use of timberlands, the protection of endangered species, the promotion of forest health and the response to and prevention of catastrophic wildfires could also affect timber supplies. Availability of harvested timber may further be limited by fire, insect infestation, disease, ice storms, wind storms, flooding and other causes, thereby reducing supply and increasing prices. Demand for OCC, especially from China, could result in shortages or spikes in the cost of OCC.

Industry supply of commodity paper and wood products is also subject to fluctuation, as changing industry conditions can influence producers to idle or permanently close individual machines or entire mills. In addition, to avoid substantial cash costs in connection with idling or closing a mill, some producers will choose to continue to operate at a loss, sometimes even a cash loss, which could prolong weak pricing environments due to oversupply. Oversupply in these markets can also result from producers introducing new capacity in response to favorable short-term pricing trends. Industry supply of commodity papers and wood products is also influenced by overseas production capacity, which has

Table of Contents

grown in recent years and is expected to continue to grow. Wood fiber pricing is subject to regional market influences, and the cost of wood fiber may increase in particular regions due to market shifts in those regions. In addition, the ability to obtain wood fiber from foreign countries may be impacted by economic, legal and political conditions in those countries as well as transportation difficulties.

Energy is a significant input cost for the paper and packaging industry. Increases in energy prices can be expected to adversely impact businesses. Energy prices, particularly for electricity, coal and fuel oil, have been volatile in recent years and currently coal and electricity prices exceed historical averages. These fluctuations have historically impacted manufacturing costs of companies in the industry, often contributing to reduced margins and increased earnings volatility. In addition, we could be materially adversely impacted by supply disruptions or the inability to pass on cost increases to our customers.

***Disruptions in transportation could adversely affect our supply of raw materials and/or our ability to distribute our products and could have an adverse effect on our results of operations, profitability and liquidity.***

Since we distribute our products by truck, rail, and ship, the reduced availability of those modes of transportation could limit our ability to promptly deliver products to our customers. The delay or failure to deliver our products to customers in a timely manner may require us to offer price concessions, discounts or other financial incentives to any affected customer in compensation for such delay or failure or could result in lost sale(s) and, ultimately, if the delay or failure is not promptly remedied, the loss of affected customers. Reduced availability of transportation could also affect our ability to receive adequate supplies of raw materials in a timely manner; which could have an adverse effect on our operations; financial condition and liquidity. In addition, the increased costs of transportation may reduce our profitability if we are not able to recover those costs through price increases for our products.

Our business in the past has been and in the future could be adversely affected by strikes and labor renegotiations affecting seaports, labor disputes between railroads or trucking companies and their union employees, or by a work stoppage at one or more seaports, railroads or local trucking companies servicing the areas in which we operate or with whom we do business.

***Paper and packaging companies face strong competition.***

We face competition from numerous competitors, domestic as well as foreign. Some of our competitors are larger, more vertically integrated companies that have greater financial and other resources, greater manufacturing economies of scale, greater energy self-sufficiency and/or lower operating costs.

***Certain paper and wood products are vulnerable to long-term declines in demand due to competing technologies or materials.***

Companies in the paper and packaging industry are subject to possible declines in demand for their products as the use of alternative materials and technologies grows and the prices of such alternatives become more competitive. Any substantial shift in demand from wood and paper products to competing technologies or materials could result in a material decrease in sales of our products and could adversely affect our results of operations, cash flows and financial position. We cannot ensure that any efforts we might undertake to adapt our product offerings to such changes would be successful or sufficient.

Table of Contents

***Paper and packaging companies are subject to significant environmental regulation and environmental compliance expenditures, as well as other potential environmental liabilities.***

Companies in the paper and packaging industry are subject to a wide range of general and industry specific environmental laws and regulations, particularly with respect to air emissions, wastewater discharges, solid and hazardous waste management, hazardous substance reporting, hazardous substance release notification, site remediation, forestry operations and endangered species habitats. We may incur substantial expenditures to maintain compliance with applicable environmental laws and regulations (or new interpretations thereof), which could adversely affect our results of operations. Failure to comply with applicable environmental laws and regulations could expose us to civil or criminal fines or penalties or enforcement actions, including orders limiting operations or requiring corrective measures, installation of pollution control equipment or other remedial actions.

**Risks Associated with Acquisitions**

***The anticipated benefits of the Longview acquisition may not be realized.***

We acquired Longview with the expectation that the acquisition of Longview would result in various benefits including, among other things, benefits relating to enhanced revenues, a broader array of product offerings, the expansion of our production capabilities, operational improvements and a diversification of our customer base. The acquisition presents challenges to management, including the integration of operations, information systems, properties and personnel of Longview and our existing operations. Achieving the anticipated benefits of the acquisition is subject to a number of uncertainties, including, but not limited to, whether we can integrate our business and the Longview business in an efficient and effective manner. Failure to achieve these anticipated benefits could result in increased costs, decreases in the amount of expected revenues and diversion of management's time and energy and could materially impact our business, financial condition and operating results.

***Future acquisitions of businesses by us would subject us to additional business, operating and industry risks, the impact of which cannot presently be evaluated, and could adversely impact our capital structure.***

We may pursue other acquisition opportunities in an effort to diversify our investments and/or grow our business. Any business acquired by us may cause us to be affected by numerous risks inherent in the acquired business' operations. If we acquire a business in an industry characterized by a high level of risk, we may be adversely affected by the currently unascertainable risks of that industry. We cannot ensure that we would be able to properly ascertain or assess all of the significant risk factors with any such acquisitions.

In addition, the financing of any acquisition completed by us could adversely impact our capital structure as any such financing would likely include the issuance of additional equity securities and/or the borrowing of additional funds. The issuance of additional equity securities may significantly dilute our stockholders and/or adversely affect prevailing market prices for our common stock. Increasing our indebtedness could increase the risk of a default that would entitle the holder to declare all of such indebtedness due and payable and/or to seize any collateral securing the indebtedness. In addition, default under one debt instrument could in turn permit lenders under other debt instruments to declare borrowings outstanding under those other instruments to be due and payable pursuant to cross default clauses. Accordingly, the financing of future acquisitions could adversely impact our capital structure and the value of your equity interest in us.

Except as required by law or the rules of any securities exchange on which our securities might be listed at the time we seek to consummate a subsequent acquisition, stockholders will not be asked to vote on any such proposed acquisition and no redemption rights in connection with any such acquisition will exist.

**Item 1B. Unresolved Staff Comments**

None.

Table of Contents**Item 2. Properties**

The table below provides a summary of our paper mills, the principal products produced and each mill's annual practical maximum capacity based upon all of our paper machines' production capabilities, as reported to the AF&PA:

Location	Products	Capacity (tons)
Longview, WA	Containerboard / Specialty Paper	1,300,000
North Charleston, SC	Containerboard / Specialty Paper	910,000
Roanoke Rapids, NC	Containerboard / Specialty Paper	460,000
Cowpens, SC	Recycled containerboard	240,000
<b>Total</b>		<b>2,910,000</b>

We have granted mortgages on all of our owned real property, including our paper mills, to secure our obligations under our Credit Facility.

As of December 31, 2014, our corrugated products production facilities included:

Corrugated Products Manufacturing Plants	Approx. Sq. Ft.	Property Leased(1)/ Owned
<b>Full-Line Box Plants</b>		
Amsterdam, NY	227,000	Leased
Bowling Green, KY	306,000	Leased
Cedar Rapids, IA	386,000	Leased
College Park, GA	183,000	Owned
Longview, WA	241,000	Owned
Mesquite, TX	275,000	Leased
Minneapolis, MN	275,000	Leased
Oakland, CA	216,000	Owned
Seattle, WA	132,000	Owned
Spanish Fork, UT	519,000	Owned
Twin Falls, ID	446,000	Owned
Yakima, WA	420,000	Owned
<b>Sheet Plants</b>		
Atlanta, GA	113,000	Leased
Aurora, IL	198,000	Leased
Cedar City UT	143,000	Owned
Grand Forks, ND	85,000	Leased
Seward, NE	85,000	Leased
Somerset, KY	87,000	Leased
Springfield, MA	235,000	Owned
<b>Sheet Feeders</b>		
Atlanta, GA	133,000	Leased
Fort Worth, TX	100,000	Owned

(1) Of the leased property 1.4 million square feet expire in 2032. The equipment in the leased facilities is, in virtually all cases, owned by KapStone, except for forklifts, trailers and other rolling stock which are leased.

We currently lease space for our corporate headquarters in Northbrook, Illinois. The lease for this facility expires in 2020.

Table of Contents

We currently believe that our owned and leased space for facilities and properties are sufficient to meet our operating requirements for the foreseeable future.

**Item 3. Legal Proceedings**

We are from time to time subject to various administrative and legal investigations, claims and proceedings incidental to our business, including environmental and safety matters, labor and employment matters, personal injury claims, contractual disputes and taxes. We establish reserves for claims and proceedings when it is probable that liabilities exist and where reasonable estimates can be made. We also maintain insurance that may limit our financial exposure for defense costs, as well as liability, if any, for claims covered by the insurance (subject also to deductibles and self-insurance amounts). While any investigation, claim or proceeding has an element of uncertainty, and we cannot predict or assure the outcome of any claim or proceeding involving the Company, we believe the outcome of any pending or threatened claim or proceeding (other than those that cannot be assessed due to their preliminary nature), or all of them combined, will not have a material adverse effect on our results of operations, cash flows or financial condition.

**Item 4. Mine Safety Disclosure**

Not applicable.

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

Our common stock, par value \$0.0001 per share, trades on the New York Stock Exchange ("NYSE") under the symbol "KS". As of December 31, 2014, there were 8 shareholders of record of our common stock. The number of shareholders of record includes one single shareholder, Cede & Co., for all of the shares held by our shareholders in individual brokerage accounts maintained at banks, brokers and institutions.

On December 11, 2013, the board of directors declared a two-for-one stock split in the form of a stock dividend (the "Stock Split"). To implement the stock split, one share of common stock for each then outstanding share of common stock was distributed on January 7, 2014 to all shareholders of record as of the close of business on December 23, 2013.

The following table sets forth the high and low sales price information for the Company's common stock from January 1, 2013 through December 31, 2014, as reported by the NYSE. All amounts for 2013 have been restated for the 2014 Stock Split (defined below).

Quarter Ended	2014		2013	
	Low	High	Low	High
March 31	\$ 26.71	\$ 32.59	\$ 11.28	\$ 13.93
June 30	\$ 24.74	\$ 33.34	\$ 13.18	\$ 20.42
September 30	\$ 28.13	\$ 33.35	\$ 20.72	\$ 24.68
December 31	\$ 24.46	\$ 31.56	\$ 21.74	\$ 28.53

At December 31, 2014, the closing share price on the NYSE was \$29.31.

In December 2014, our board of directors approved the initiation of a regular quarterly dividend of \$0.10 per share, indicating a current annualized dividend of \$0.40 per share. The timing and amount of future dividends are subject to the determination of the Company's board of directors.

There were no cash dividends or other cash distributions made during 2013.

Table of Contents

**Stock Performance Graph**

The performance graph shall not be deemed to be "soliciting material" or to be "filed" with the commission or subject to Regulation 14A or 14C, or to the liabilities of Section 18 of the Securities Exchange Act of 1934 as amended.

The following graph compares a \$100 investment in our common stock on December 31, 2009 with a \$100 investment in each of the S&P 500 and the S&P Paper and Packaging Index (the Company's peer group) also made on December 31, 2009. The graph portrays total return, 2009-2014, assuming reinvestment of dividends.

**Comparison of 5 Year Cumulative Total Return  
Assumes Initial Investment of \$100  
December 2014**



Table of Contents**Item 6. Selected Financial Data**

The following table sets forth KapStone's selected financial information derived from its audited consolidated financial statements as of, and for the years ended, December 31, 2014, 2013, 2012, 2011 and 2010.

The selected financial data presented below summarizes certain financial data which has been derived from and should be read in conjunction with Item 7. "Management's Discussion and Analysis of Financial Condition and Results of Operations" and KapStone's audited consolidated financial statements included in Item 8.

In thousands, except per share amounts	Years Ended December 31,				
	2014	2013(1)	2012	2011(1)	2010
<b>Statement of Income Data:</b>					
Net sales	\$ 2,300,920	\$ 1,748,162	\$ 1,216,637	\$ 906,119	\$ 782,676
Operating income(2)	\$ 299,931	\$ 219,888	\$ 109,560	\$ 106,741	\$ 68,703
Net income(3)	\$ 171,915	\$ 127,338	\$ 62,505	\$ 123,981	\$ 65,041
Basic net income per share(4)	\$ 1.79	\$ 1.34	\$ 0.67	\$ 1.34	\$ 0.71
Diluted net income per share(4)	\$ 1.76	\$ 1.32	\$ 0.65	\$ 1.31	\$ 0.69
Cash dividends declared per common share(5)	\$ 0.10	\$	\$ 1.00	\$	\$
<b>Balance Sheet Data:</b>					
Cash and cash equivalents	\$ 28,467	\$ 12,967	\$ 16,488	\$ 8,062	\$ 67,358
Total assets	\$ 2,556,274	\$ 2,651,862	\$ 1,135,860	\$ 1,130,147	\$ 723,421
Long-term liabilities	\$ 1,499,338	\$ 1,715,504	\$ 414,628	\$ 442,269	\$ 185,539
Total stockholders' equity	\$ 778,127	\$ 666,080	\$ 517,948	\$ 546,278	\$ 418,634

- (1) 2013 results reflect the results of the Longview acquisition on July 18, 2013 while 2011 results and later reflect the USC acquisition on October 31, 2011.
- (2) 2009 and 2010 operating income includes \$164.0 million and \$22.2 million, respectively, of income from alternative fuel mixture credits.
- (3) 2013 and 2011 net income includes a \$5.0 million and \$63.0 million benefit, respectively, from the reversal of the tax reserves for alternative fuel mixture credits. 2010 net income includes a \$21.0 million cellulosic biofuel producers' tax credit.
- (4) Earnings per share for all periods have been restated for the stock split declared in December 2013.
- (5) In December 2014, the Company declared a regular dividend that will be paid in January 2015. In December 2012, the Company paid a special cash dividend.

See Note 3 in the Notes to Consolidated Financial Statements for a discussion of the Longview acquisition.

Table of Contents

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

**Executive Summary**

Net sales of \$2.3 billion and earnings of \$171.9 million in 2014 were both a record high for the Company reflecting 2.8 million tons of product sold. In 2014, the average mill selling price per ton increased by \$15 to \$684 per ton. This increase was primarily due to the realization of 2013 containerboard and corrugated products price increases, along with 2013 specialty paper price increases, and the 2014 kraft paper price increase. Our mill operations had a strong year in 2014, producing a record 2.7 million tons of containerboard and specialty paper compared to 2.1 million tons in 2013.

Some key highlights for 2014 include:

In February the Company completed a \$29 million investment at our North Charleston mill. The primary project in this investment was the replacement of the press section on No. 3 Paper Machine, which is designed to improve the capability and efficiency of producing Ultra High Performance (UPL) lightweight linerboard grades.

In March the Company announced a \$50 per ton selling price increase for kraft paper. This price increase was fully realized by the end of the third quarter of 2014.

In July the Company released its 2013 sustainability report, which showed significant progress toward its 2020 sustainability goals. These goals, which were set based on our commitment to social responsibility, extend well beyond applicable laws and regulations mandated by federal, state and local governmental entities.

In September the Company entered into an accounts receivable securitization arrangement ("Securitization") with Wells Fargo Bank, N.A. and PNC Bank, N.A. The Securitization generated proceeds of \$175 million which were used to partially prepay our existing term loans. Due to a lower interest rate on the Securitization, our gross annual interest expense is expected to be reduced by approximately \$2.0 million.

In December the Company's board of directors approved the initiation of a regular quarterly dividend of \$0.10 per share which was paid on January 12, 2015.

As of December the Company merged its three defined benefit pension plans into one.

We believe we are the 5th largest manufacturer of containerboard in the United States.

Edgar Filing: KAPSTONE PAPER & PACKAGING CORP - Form 10-K

Table of Contents

**Results of Operations for the Years Ended December 31, 2014, 2013, and 2012**

The following table compares results of operations for the years ended December 31, 2014 and 2013:

	Years Ended December 31,			% of Net Sales	
	2014	2013	% Change	2014	2013
Net sales	\$ 2,300,920	\$ 1,748,162	31.6%	100.0%	100.0%
Cost of sales, excluding depreciation and amortization	1,551,531	1,186,930	30.7%	67.4%	67.9%
Depreciation and amortization	136,548	95,435	43.1%	5.9%	5.5%
Freight and distribution expenses	175,901	135,972	29.4%	7.6%	7.8%
Selling, general and administrative expenses	137,009	110,612	23.9%	6.0%	6.3%
Other operating income		675	(100.0)%		
Operating income	299,931	219,888	36.4%	13.0%	12.6%
Foreign exchange gain/(loss)	(1,222)	232	626.7%	(0.1)%	
Loss on debt extinguishment	5,617		100.0%	0.2%	
Interest expense, net	32,491	25,130	29.3%	1.4%	1.4%
Income before provision for income taxes	260,601	194,990	33.6%	11.3%	11.2%
Provision for income taxes	88,686	67,652	31.1%	3.9%	3.9%
Net income	\$ 171,915	\$ 127,338	35.0%	7.6%	7.3%

Net sales for the year ended December 31, 2014 were \$2,300.9 million compared to \$1,748.2 million for the year ended December 31, 2013, an increase of \$552.7 million. The increase in net sales was driven primarily by the Longview acquisition which accounted for \$510.2 million. In addition to the Longview acquisition, net sales increased by \$29.5 million due to higher average selling prices and product mix changes and \$11.1 million of higher sales volume. Average mill selling price per ton for 2014 was \$684 compared to \$669 for 2013. Average mill selling prices increased primarily due to the realization of 2013 containerboard and corrugated products price increases, along with 2013 specialty paper price increases, and the \$50 per ton 2014 kraft paper selling price increase.

The following represents the Company's sales by product line:

Product Line Revenue:	Years Ended December 31,							
	Net Sales (in thousands)		Increase/ (Decrease)	%	Tons Sold		Increase/ (Decrease)	%
	2014	2013			2014	2013		
Containerboard / Corrugated products	\$ 1,463,670	\$ 1,108,545	\$ 355,125	32.0%	1,764,628	1,403,797	360,831	25.7%
Specialty paper	741,601	551,931	189,670	34.4%	1,031,024	799,261	231,763	29.0%
Other	95,649	87,686	7,963	9.1%				
Product sold	\$ 2,300,920	\$ 1,748,162	\$ 552,758	31.6%	2,795,652	2,203,058	592,594	26.9%

Tons of product sold in 2014 was 2,795,652 tons compared to 2,203,058 tons in 2013. Excluding the Longview acquisition, tons of products sold in 2014 decreased by 14,738 tons or 0.9 percent as follows:

Containerboard / Corrugated product sales volume decreased 1.3 percent. Containerboard sales decreased 5.8 percent reflecting volumes being redirected from outside sales to fulfill demand for internal converting. Corrugated product sales volume increased 6.5 percent.

Specialty paper sales decreased by 0.1 percent, primarily due to lower Durasorb® sales, which decreased 5.8 percent, partially offset by a kraft paper volume increase of 3.2 percent.

Table of Contents

Cost of sales, excluding depreciation and amortization expense, for the year ended December 31, 2014 was \$1,551.5 million compared to \$1,186.9 million for the year ended December 31, 2013, an increase of \$364.6 million. The increase in cost of sales was mainly due to the \$337.5 million impact of the Longview acquisition. In addition to the Longview acquisition, cost of sales increased mainly due to \$21.5 million of inflation on labor, benefits and input costs, \$18.7 million of higher sales volume, \$11.2 million of higher planned maintenance outage costs, \$6.6 million of voluntary severance plan charges and \$4.4 million of other cost increases. These cost increases were partially offset by \$35.3 million of productivity gains, primarily resulting from higher production and cost savings. Including Longview, annual planned maintenance outage costs during 2014 and 2013 totaled \$36.1 million and \$24.9 million, respectively, and were included in cost of sales for those years.

Depreciation and amortization expense for the year ended December 31, 2014 totaled \$136.5 million compared to \$95.4 million for 2013. The increase of \$41.1 million was primarily due to \$34.1 million from the Longview acquisition, \$5.2 million of which reflected amortization of identified intangibles, and \$7.0 million was the result of higher capital spending.

Freight and distribution expenses for the year ended December 31, 2014 totaled \$175.9 million compared to \$136.0 million for 2013. The increase of \$39.9 million was primarily due to \$30.5 million from the Longview acquisition, \$7.5 million from higher sales volumes and mix and \$1.9 million of inflation and other cost increases.

Selling, general and administrative expenses for the year ended December 31, 2014 totaled \$137.0 million compared to \$110.6 million in 2013. The increase of \$26.4 million was primarily due to \$25.2 million from the Longview acquisition. In addition to the Longview acquisition, selling, general, and administrative expenses increased due to \$3.9 million of higher compensation and benefit related expenses, \$4.2 million of 2014 Longview integration related expenses, \$0.9 million higher legal expenses and \$0.3 million of voluntary severance plan charges, partially offset by \$8.5 million of 2013 Longview acquisition related expenses that did not occur in 2014. As a percentage of net sales, selling, general, and administrative expenses decreased to 6.0 percent in 2014 from 6.3 percent in 2013.

Loss on debt extinguishment for the year ended December 31, 2014, was \$5.6 million due to the \$325.0 million of voluntary prepayments on the term loans under the Credit Facility.

Net interest expense for the years ended December 31, 2014 and 2013 was \$32.5 million and \$25.1 million, respectively. Interest expense reflects interest on the Company's borrowings under its Credit Facility, Receivables Credit Facility and amortization of debt issuance costs. Interest expense was \$7.4 million higher for the year ended 2014 due to higher term loan balances used to fund the Longview acquisition and an increase in variable interest rates.

Provision for income taxes for the years ended December 31, 2014 and 2013 was \$88.7 million and \$67.7 million, respectively, reflecting an effective income tax rate of 34.0 percent for 2014 compared to 34.7 percent for 2013. The higher provision for income taxes in 2014 primarily reflects higher pre-tax income. In addition, 2013 included a \$5.0 million favorable adjustment for reversal of a tax reserve for an uncertain tax position relating to alternative fuel mixture credits.

Edgar Filing: KAPSTONE PAPER & PACKAGING CORP - Form 10-K

Table of Contents

The following table compares results of operations for the years ended December 31, 2013 and 2012:

	Years Ended December 31,			% of Net Sales	
	2013	2012	% Change	2013	2012
Net sales	\$ 1,748,162	\$ 1,216,637	43.7%	100.0%	100.0%
Cost of sales, excluding depreciation and amortization	1,186,930	866,124	37.0%	67.9%	71.2%
Depreciation and amortization	95,435	63,124	51.2%	5.5%	5.2%
Freight and distribution expenses	135,972	108,438	25.4%	7.8%	8.9%
Selling, general and administrative expenses	110,612	70,055	57.9%	6.3%	5.8%
Other operating income	675	664	1.7%		0.1%
<b>Operating income</b>	<b>219,888</b>	<b>109,560</b>	<b>100.7%</b>	<b>12.6%</b>	<b>9.0%</b>
Foreign exchange gain/(loss)	232	(303)	176.6%		
Interest expense, net	25,130	11,774	113.4%	1.4%	1.0%
Income before provision for income taxes	194,990	97,483	100.0%	11.2%	8.0%
Provision for income taxes	67,652	34,978	93.4%	3.9%	2.9%
<b>Net income</b>	<b>\$ 127,338</b>	<b>\$ 62,505</b>	<b>103.7%</b>	<b>7.3%</b>	<b>5.1%</b>

Net sales for the year ended December 31, 2013 were \$1,748.2 million compared to \$1,216.6 million for the year ended December 31, 2012, an increase of \$531.6 million. The increase in net sales was driven primarily by the Longview acquisition, which accounted for \$439.6 million. Excluding the Longview acquisition, net sales increased by \$92.0 million or 7.6 percent. Net sales (excluding Longview) increased by \$77.3 million due to higher average selling prices, \$9.2 million of other sales and \$5.5 million due to volume and product mix changes. Average mill selling price per ton for 2013 was \$669 compared to \$622 for 2012. Average mill selling prices increased primarily due to the full realization of the 2012 and 2013 price increases for domestic containerboard and corrugated products.

The following represents the Company's sales by product line:

Product Line Revenue:	Years Ended December 31,				Tons Sold			
	Net Sales (in thousands)		Increase/ (Decrease)	%	2013	2012	Increase/ (Decrease)	%
	2013	2012						
Containerboard / Corrugated products	\$ 1,108,545	\$ 714,085	\$ 394,460	55.2%	1,403,797	1,046,500	357,297	34.1%
Specialty paper	551,931	428,663	123,268	28.8%	799,261	633,965	165,296	26.1%
Other	87,686	73,889	13,797	18.7%				0.0%
<b>Product sold</b>	<b>\$ 1,748,162</b>	<b>\$ 1,216,637</b>	<b>\$ 531,525</b>	<b>43.7%</b>	<b>2,203,058</b>	<b>1,680,465</b>	<b>522,593</b>	<b>31.1%</b>

Tons of product sold in 2013 was 2,203,058 tons compared to 1,680,465 tons in 2012. Excluding the Longview acquisition, tons of products sold in 2013 decreased by 13,897 tons or 1 percent as follows:

Domestic containerboard sales increased 14.5 percent due to higher demand for ultra performance containerboard grades.

Corrugated product sales volume increased 3.9 percent reflecting a heavier basis weight of tons shipped and product mix, new customers and the addition of the Aurora manufacturing facility.

Export containerboard sales decreased by 30.3 percent as more containerboard volume was shipped to domestic customers and used for internal consumption.

Table of Contents

Specialty paper sales decreased by 5.7 percent, primarily due to Kraft paper sales which decreased 20.5 percent, reflecting an overall decrease in demand in the industry and lower volume of sales to a customer as it internalized its needs, partially offset by higher Durasorb® and Kraftpak® volume.

Cost of sales, excluding depreciation and amortization expense, for the year ended December 31, 2013 was \$1,186.9 million compared to \$866.1 million for the year ended December 31, 2012, an increase of \$320.8 million. The increase in cost of sales was mainly due to the \$272.0 million impact of the Longview acquisition. Excluding the Longview acquisition, cost of sales increased by \$48.8 million, or 5.6 percent, mainly due to \$32.5 million of inflation on labor, benefits and input costs, \$6.5 million of higher planned maintenance outage costs and other cost increases. Including Longview, annual planned maintenance outage costs during 2013 and 2012 totaled \$24.9 million and \$18.4 million, respectively, and were included in cost of sales for those years.

Depreciation and amortization expense for the year ended December 31, 2013 totaled \$95.4 million compared to \$63.1 million for 2012. The increase of \$32.3 million was primarily due to \$27.6 million from the Longview acquisition, \$2.4 million of which was amortization of identified intangibles. Excluding the Longview acquisition, depreciation and amortization expense increased \$5.3 million due to the recent investments in information technology, equipment upgrades, and replacements at the paper mills.

Selling, general and administrative expenses for the year ended December 31, 2013 totaled \$110.6 million compared to \$70.1 million in 2012. The increase of \$40.5 million was primarily due to \$26.1 million from the Longview acquisition. Excluding the Longview acquisition, selling, general, and administrative expenses increased by \$14.4 million due to \$8.5 million of Longview transaction fees and expenses, \$5.9 million of higher compensation related expenses, \$1.8 million of higher IT and consulting expenses, \$1.4 million for the Aurora, IL manufacturing facility, and \$0.6 million of bad debt expense, partially offset by \$3.8 million of 2012 USC acquisition and integration related expenses. As a percentage of net sales, selling, general, and administrative expenses increased to 6.3 percent in 2013 from 5.8 percent in 2012.

Net interest expense for the years ended December 31, 2013 and 2012 was \$25.1 million and \$11.8 million, respectively. Interest expense reflects interest on the Company's borrowings under its Credit Facility and amortization of debt issuance costs. Interest expense was \$13.3 million higher for the year ended 2013 due to higher term loan balances used to fund the Longview acquisition and an increase in variable interest rates.

Provision for income taxes for the years ended December 31, 2013 and 2012 was \$67.7 million and \$35.0 million, respectively, reflecting an effective income tax rate of 34.7 percent for 2013 compared to 35.9 percent for 2012. The higher provision for income taxes in 2013 primarily reflects higher pre-tax income and higher state income taxes, partially offset by a \$5.0 million favorable adjustment for reversal of a tax reserve for an uncertain tax position relating to alternative fuel mixture credits.

**Liquidity and Capital Resources**

***Receivables Credit Facility***

In September 2014, certain wholly-owned subsidiaries of the Company ("Originators") entered into a one-year agreement to sell all eligible trade receivables (the "Receivables") on a non-recourse basis (subject to purchase price credits for breaches of certain representations and warranties with respect to the Receivables), to KapStone Receivable, LLC ("KAR"), a wholly-owned subsidiary of the Company that is a bankruptcy remote variable interest entity (the "VIE"). KAR is a variable interest entity as it receives subordinated financing from the Originators from time to time to finance its activities. The Company continues to service the receivables after they have been sold to KAR and makes the



Table of Contents

primary decisions regarding the collateral in KAR and is therefore the primary beneficiary and will consolidate the account balances of KAR. KAR finances its purchases of the Receivables in part with proceeds of draws under a one-year facility ("Receivables Credit Facility"), subject to a maximum of \$175 million. The actual amount available to draw upon varies based on eligible receivables (as defined in the agreement establishing the Receivables Credit Facility). The proceeds from the initial sales of the Receivables were used to pay down the term loans under our Amended and Restated Credit Agreement. As of December 31, 2014, \$167.0 million was outstanding with an interest rate of 0.9 percent.

***Amendments to the Amended and Restated Credit Agreement***

In April 2014, the Company entered into a First Amendment (the "First Amendment") to the Amended and Restated Credit Agreement dated as of July 18, 2013 (as amended from time to time, the "Amended and Restated Credit Agreement"). The First Amendment reduced the borrowing rates under our Credit Facility for both term loans under the Credit Facility and for any future borrowings under the \$400 million revolving credit facility (the "Revolver") portion of the Credit Facility. The interest rates are based on LIBOR rates plus a margin determined from a pricing grid based on the Company's debt to EBITDA ratio as defined in our Amended and Restated Credit Agreement. Accordingly, the weighted average interest rate on borrowings under the Credit Facility as of December 31, 2014 is 1.98 percent, compared to 2.25 percent as of March 31, 2014. The First Amendment also reduced the unused commitment fees related to the Revolver by 5 to 10 basis points.

In August 2014, the Company entered into a Second Amendment to the Amended and Restated Credit Agreement, which included certain technical amendments to the Amended and Restated Credit Agreement in connection with the Receivables program and the related Receivables Credit Facility.

In December 2014, the Company entered into a Third Amendment to the Amended and Restated Credit Agreement. The modification of the Amended and Restated Credit Agreement will enable the Company, subject to certain conditions and limitations, to pay dividends on, or make repurchases of, the Company's common stock.

***Voluntary and Mandatory Prepayments***

For the year ended December 31, 2014, the Company made \$325.0 million of voluntary prepayments on its term loans under its credit facility using \$175.0 million of cash from the Receivables Credit Facility and \$150.0 million of cash generated from operations.

For the year ended December 31, 2014, the Company made an \$8.0 million mandatory payment on the Receivable Credit Facility based on the Company's eligible receivables. No mandatory prepayments were required under the Amended and Restated Credit Agreement.

For the year ended December 31, 2013, the Company made a \$40.0 million voluntary prepayment on its term loan under its then-existing credit agreement using cash generated from operations.

***Other Borrowing***

In 2014 and 2013, the Company entered into financing agreements of \$6.3 million and \$5.1 million, respectively, at an annual interest rate of 1.69 and 1.61 percent, respectively, for its annual property insurance premiums. These agreements required the Company to pay consecutive monthly payments through the term of each financing agreement ending on December 1<sup>st</sup> of each year. The Company entered into a similar agreement in 2015 with quarterly payment terms ending on October 15<sup>th</sup>.

Table of Contents**Debt Covenants**

Under the financial covenants of the Amended and Restated Credit Agreement, the Company must comply on a quarterly basis with a maximum permitted leverage ratio. The leverage ratio is calculated by dividing the Company's debt by its rolling twelve month total earnings before interest expense, taxes, depreciation and amortization and allowable adjustments. The maximum permitted leverage ratio declines over the life of the Amended and Restated Credit Agreement. On December 31, 2014, the maximum permitted leverage ratio was 4.25 to 1.00. On December 31, 2014, the Company was in compliance with a leverage ratio of 2.38 to 1.00.

The Amended and Restated Credit Agreement also includes a financial covenant requiring a minimum fixed charge coverage ratio. This ratio is calculated by dividing the Company's twelve month total earnings before interest expense, taxes, depreciation and amortization and allowable adjustments less cash payments for income taxes and capital expenditures by the sum of our cash interest and required principal payments during the twelve month period. From the closing date of the Amended and Restated Credit Agreement through the quarter ending December 31, 2014, the fixed charge coverage ratio was required to be at least 1.25 to 1.00. On December 31, 2014, the Company was in compliance with the Amended and Restated Credit Agreement with a fixed charge coverage ratio of 7.53 to 1.00.

As of December 31, 2014, Company was also in compliance with all other covenants in the Amended and Restated Credit Agreement.

**Income Taxes**

Income taxes paid, net of refunds, were \$77.5 million, \$4.0 million and \$7.0 million in 2014, 2013 and 2012, respectively. The increase in 2014 is primarily due to higher pre-tax income following the 2013 Longview acquisition, significant tax credit carry-forwards and net operating losses fully utilized through 2013 and bonus depreciation claimed in 2013. The Company expects its 2015 cash tax rate to be approximately 35 percent.

**Sources and Uses of Cash**

Years ended December 31 (\$ in thousands)	2014	2013	2012
Operating activities	\$ 313,198	\$ 298,694	\$ 157,829
Investing activities	(137,232)	(634,945)	(67,551)
Financing activities	(160,466)	332,730	(81,852)
Total change in cash and cash equivalents	\$ 15,500	\$ (3,521)	\$ 8,426

**2014**

Cash and cash equivalents increased by \$15.5 million from December 31, 2013, reflecting \$313.2 million of net cash provided by operating activities, \$137.2 million of net cash used in investing activities and \$160.5 million of net cash used by financing activities.

Net cash provided by operating activities was \$313.2 million, comprised primarily of net income of \$171.9 million and non-cash charges of \$147.4 million. Changes in operating assets and liabilities used \$6.1 million of cash. Net cash provided by operating activities increased by \$14.5 million during the year ended December 31, 2014 compared to 2013 mainly due to a \$44.6 million increase in net income, which was partially offset by \$18.9 million of cash used for working capital and lower non-cash charges of \$11.2 million.

Table of Contents

Net cash used in investing activities was \$137.2 million for capital expenditures. For the year ended December 31, 2014, capital expenditures included \$49.5 million for our Longview operations acquired on July 18, 2013 and \$5.6 million for the completion of the North Charleston, South Carolina paper mill No. 3 paper machine upgrade. Capital expenditures increased by \$40.5 million in 2014 compared to 2013 due to the Longview acquisition and higher strategic capital spending.

Net cash used in financing activities was \$160.5 million and reflects \$325.0 million of voluntary prepayments on the term loans under the Credit Facility, \$8.0 million repayment on the Receivables Credit Facility as a result of a reduction in the Company's eligible receivables, \$3.5 million for principal payments on the term loans, \$1.1 million of fees paid for the Receivables Credit Facility and the First Amendment, and \$0.2 million for cash dividends paid. These amounts were partially offset by \$175.0 million of initial proceeds from Receivables Credit Facility and \$2.4 million of proceeds from share transactions. Net cash provided by financing activities decreased by \$493.2 million in 2014 compared to 2013, primarily due to higher net borrowings in 2013 as a result of the Longview acquisition.

**2013**

Cash and cash equivalents decreased by \$3.5 million from December 31, 2012, reflecting \$298.7 million of net cash provided by operating activities and \$332.7 million of net cash provided by financing activities, offset by cash used in investing activities of \$634.9 million.

Net cash provided by operating activities was \$298.7 million due to non-cash charges of \$158.6 million, net income of \$127.3 million and changes in operating assets and liabilities of \$12.8 million. Net cash provided by operating activities increased by \$140.9 million during the year ended December 31, 2013 compared to 2012 mainly due to higher non-cash charges of \$69.0 million, higher net income of \$64.8 million and \$7.1 million of cash provided by changes in operating assets and liabilities.

Net cash used in investing activities includes \$538.2 million for the Longview acquisition and \$96.7 million of capital expenditures. For the year ended December 31, 2013, capital expenditures included \$10.2 million for the new manufacturing facility in Aurora, IL and \$22.2 million for Longview. Net cash used in investing activities increased by \$567.4 million in 2013 compared to 2012, primarily due to the Longview acquisition.

Net cash provided by financing activities totaled \$332.7 million, reflecting \$1,275.0 million of borrowings under the Credit Facility, partially offset by the \$812.8 million payoff of the Company's prior credit facility and Longview's senior notes assumed in the acquisition, \$63.5 million of short-term borrowing repayments, a \$40.0 million voluntary prepayment, \$19.7 million of debt issuance costs for the Amended and Restated Credit Agreement and a \$11.2 million scheduled principal payment. Net cash provided by financing activities increased by \$414.6 million in 2013 compared to 2012, mainly due to higher net borrowings in 2013 due to the Longview acquisition.

***Future Cash Needs***

We expect that cash on hand at December 31, 2014 and cash generated from operating activities in 2015 and, if needed, the ability to draw from our \$400.0 million Revolver and our \$300.0 million accordion provision under our Credit Facility, if available, will be sufficient to meet anticipated cash needs, which primarily consists of \$21.2 million of interest payments on our term loans, approximately \$135.0 million of expected capital expenditures, \$38.4 million of dividends, \$1.1 million of pension plan funding and any additional working capital needs.

At December 31, 2014, the Company had no borrowings under the Revolver and had \$395.7 million of remaining revolver availability net of outstanding letters of credit.

Table of Contents

On a long term basis, we expect that cash generated from operating activities and, if needed, the ability to draw from our Revolver and accordion provision, if available, will be sufficient to meet long term obligations. Our long term obligations primarily consist of \$1.1 billion of debt service and interest (which includes a \$513.2 million final payment on our term loan A-1 and \$167.0 million on our Receivable Credit Facility in July 2018 and a final payment on our term loan A-2 in July 2020 of \$231.1 million), capital expenditures of \$110.0 to \$125.0 million annually, annual defined benefit pension plan contributions, dividends, and working capital needs and acquisitions.

**Off-Balance Sheet Arrangements**

We have not entered into any off-balance sheet financing arrangements. The Company established a variable interest entity in connection with the Receivables Credit Facility. We have not guaranteed any debt or commitments of other entities or entered into any options on non-financial assets.

**Critical Accounting Policies**

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 at the date of the financial statements and the reported amounts of expenses during the reporting period. Actual results could differ from those estimates. We believe our critical accounting policies are those described below. The Company's audit committee has reviewed the policies listed below. For a detailed discussion of these and other accounting policies, see Note 2 "*Significant Accounting Policies*" of the Notes to the Consolidated Financial Statements.

***Revenue Recognition***

The Company recognizes revenue in accordance with Accounting Standards Codification ("ASC") 605, *Revenue Recognition*. Revenue is recognized when the customer takes title and assumes the risks and rewards of ownership. Sales with terms designated f.o.b. (free on board) shipping point are recognized at the time of shipment. For sales transactions with terms f.o.b. destination, revenue is recorded when the product is delivered to the customer's site and when title and risk of loss are transferred. Sales on consignment are recognized in revenue at the earlier of the month that the goods are consumed or after a period of time subsequent to receipt by the customer as specified by contract terms. Incentive rebates are typically paid in cash and are netted against revenue on an accrual basis as qualifying purchases are made by the customer to earn and thereby retain the rebate.

The Company recognizes revenue from the sale of shaft horsepower, generated by its cogeneration facility, and energy sales on a gross basis and is included in net sales.

Freight charged to customers is recognized in net sales.

***Goodwill and Intangibles***

Certain business acquisitions have resulted in the recording of goodwill. Upon acquisition, the purchase price is first allocated to identifiable assets and liabilities based on estimated fair value, with any remaining purchase price recorded as goodwill. Goodwill is considered an indefinite lived intangible asset and as such is not amortized. At December 31, 2014, we have goodwill of \$533.9 million. In conjunction with the Longview acquisition the Company's goodwill increased by \$308.3 million, see Note 3 "*Longview Acquisition*" of the Notes to Consolidated Financial Statements.

***Goodwill Valuations***

We evaluate goodwill using a qualitative assessment to determine whether it is more likely than not that the fair value of any reporting unit is less than its carrying amount. If we determine that the

Table of Contents

fair value of the reporting unit may be less than its carrying amount, we evaluate goodwill using a two-step impairment test. Otherwise, we conclude that no impairment is indicated and we do not perform the two-step impairment test.

In conducting a qualitative assessment, the Company analyzes a variety of events or factors that may influence the fair value of the reporting unit, including, but not limited to: the results of prior quantitative tests performed; changes in the carrying amount of the reporting unit; actual and projected operating results; relevant market data for both the Company and its peer companies; industry outlooks; macroeconomic conditions; liquidity; changes in key personnel; and the Company's competitive position. Significant judgment is used to evaluate the totality of these events and factors to make the determination of whether it is more likely than not that the fair value of the reporting unit is less than its carrying value.

If the qualitative assessment concludes that the two-step impairment test is necessary, we first compare the book value of a reporting unit, including goodwill, with its fair value. The fair value is estimated based on a market approach and a discounted cash flow analysis, also known as the income approach, and is reconciled back to the current market capitalization for the Company to ensure that the implied control premium is reasonable. If the book value of a reporting unit exceeds its fair value, we perform the second step to estimate an implied fair value of the reporting unit's goodwill by allocating the fair value of the reporting unit to all of the assets and liabilities other than goodwill (including any unrecognized intangible assets). The difference between the total fair value of the reporting unit and the fair value of all the assets and liabilities other than goodwill is the implied fair value of that goodwill. The amount of impairment loss is equal to the excess of the book value of the goodwill over the implied fair value of that goodwill.

***Evaluating Goodwill Results and Significant Assumptions***

Based on the favorable results of the qualitative assessment conducted as of October 1, 2014, there was no goodwill impairment charge recorded in 2014.

For our three reporting units our qualitative assessment included a review of the events and factors outlined above. Significant weight was provided to the following factors, as we determined that these items have the most significant impact on the fair value of this reporting unit.

**Market valuation** This factor best reflects a market participant view of the Company. The substantial increase of approximately \$500 million from the prior year is directly attributable to the improved legacy performance, Longview integration, and is a positive indicator of no impairment.

**Actual 2014 operating performance vs. expectations** the Company's ability to execute and deliver performance in excess of projections during 2014 reflects management's ability to adapt to market conditions and deliver record operating results.

The discount rate used for the last performed quantitative assessment in 2012 was 10.5 percent. Since then the Company estimates that the discount rate has decreased to 9.0 percent in 2014 based on analysis prepared with the assistance of a third party. An overall decrease in the discount rate has a favorable impact to fair values of the reporting units.

**Better expected future performance** partially due to a full year realization of the \$50 per ton 2014 kraft paper selling price increase and productivity improvements from the Company's 2014 strategic capital expenditures.

Intangible assets acquired in a business combination or asset purchase are initially valued at the fair market value using generally accepted valuation methods appropriate for the type of the intangible asset. Definite-lived intangible assets are amortized over their estimated useful lives and are reviewed

Table of Contents

for impairment if indicators of impairment arise. The evaluation of the impairment is based upon a comparison of the carrying amount of the intangible asset to the estimated future undiscounted cash flows expected to be generated by the asset. If the estimated undiscounted future cash flows are less than the carrying amount of the assets, the asset is considered to be impaired. If impaired, the intangible asset is written down to estimated fair market value.

**Pension Benefits**

The Company provides pension benefits to certain employees and accounts for these benefits in accordance with ASC 715, *Compensation Retirement Benefits*. For financial reporting purposes, assumptions are developed through consultations with investment advisors and actuaries for expected long-term rate of return on plan assets, discount rates and mortality rates. There is authoritative guidance on how to select most of these assumptions, however, management exercises judgment when deciding on the final assumptions used for valuation purposes. We evaluated the assumptions for the year ended December 31, 2014 and we believe they are within accepted industry ranges, although an increase or decrease in the assumptions or economic events outside our control could have a direct impact on future recorded obligations and reported net earnings. A summary of key assumptions for 2014, 2013 and 2012 is as follows:

	<b>Pension Benefits Actuarial Assumptions</b>		
	<b>2014</b>	<b>2013</b>	<b>2012</b>
Weighted-average discount rate assumption used to determine PBO at December 31,	4.24%	5.11%	4.11%
Weighted-average actuarial assumptions for net expense:			
Discount rate	5.11%	4.77%	4.64%
Long-term rate of return on plan assets	6.98%	6.25%	6.50%

The measurement date for our plan is year-end as of December 31. Accordingly, at the end of each year; we determine the discount rate to be used to discount pension liabilities to its present value. This rate is adjusted to match the duration of the liabilities associated with the pension plan. The discount rate reflects the current rate at which the pension liabilities could be effectively settled at the end of the year. The Company's estimate of its projected benefit obligation ("PBO") is highly dependent on changes in market interest rates. In estimating this rate at the end of 2014, we reviewed rates of return on relevant market indices and concluded that the Fidelity Bond Modeler is consistent with observable market conditions and industry standards for developing spot rate curves. The impact of the change in market interest rates during 2014 from the prior year resulted in a \$66.3 million increase to our December 31, 2014 projected benefit obligation ("PBO") and was recorded through "Accumulated other comprehensive income / (loss)," a component of "Stockholders' Equity" in the Consolidated Balance Sheets.

A significant element in determining our net periodic benefit income is the expected return on plan assets. For 2014, we had assumed that the expected long-term rate of return on plan assets would be 6.98 percent, or \$44.1 million. This expected return on plan assets is included in the net periodic benefit income for the year ended December 31, 2014. As a result of the combined effect of valuation changes in both the equity and bond markets, the actual return on plan assets was approximately 5.8 percent, or \$37.9 million in 2014. The difference between the expected return and the actual return on plan assets is reflected on the Consolidated Balance Sheets through charges to "Accumulated other comprehensive income / (loss)." As of December 31, 2014 and 2013, the fair value of plan assets is \$647.5 million and \$645.5 million, respectively.

Table of Contents

In addition to the change from the prior year in discount rates, we adopted new U.S. mortality tables in 2014 for purposes of determining our mortality assumption used in the defined benefit plan's liability calculation. The new assumptions were based on the Society of Actuaries' recent mortality experience study and reflect future mortality improvement. Based on our experience and in consultation with our actuaries, we utilized a base RP-2014 with MP-2014 projection scale and appropriate collar adjustments. In 2013, we utilized the RP-2000 mortality tables. The updated mortality assumption resulted in an increase to the projected benefit obligation of \$27.8 million as of the end of 2014 and was recorded through "Accumulated other comprehensive income / loss," a component of "Stockholders' Equity" in the Consolidated Balance Sheets.

As of December 31, 2014 and 2013, we determined the discount rate for our plan to be 4.24 percent and 5.11 percent, respectively, and used these rates to measure the PBO at the end of each respective year end. The decrease in the discount rate, the change to the updated mortality assumption, and overall plan experience has increased the PBO, by \$91.5 million to \$669.2 million as of December 31, 2014 from \$577.7 million as of December 31, 2013. The Plan's unfunded status was \$21.7 million as of December 31, 2014 compared to a surplus of \$67.8 million as of December, 31 2013.

We recognized net periodic pension income of \$5.0 million in 2014, compared to \$1.3 million of net periodic pension expense in 2013. For the year ended December 31, 2015, we estimate net periodic pension income to approximate \$6.1 million reflecting a discount rate of 4.24 percent and an expected return on plan assets of 6.5 percent.

***Income Taxes***

The Company accounts for income taxes under the liability method in accordance with ASC 740, *Income Taxes*. Accordingly, deferred income taxes are provided for the future tax consequences attributable to differences between the carrying amounts of assets and liabilities for financial reporting and income tax purposes. Deferred tax assets and liabilities are measured using tax rates in effect for the year in which those temporary differences are expected to be recovered or settled. A valuation allowance is established when necessary to reduce deferred tax assets to the amount that is more likely than not to be realized. The Company recognizes the benefit of tax positions when it is more likely than not to be sustained on its technical merits. The Company records interest and penalties on unrecognized tax benefits in the provision for income taxes. As of December 31, 2014, the Company does not have any valuation allowances.

**Recent Accounting Pronouncements**

See Note 2 "*Significant Accounting Policies*" in the Notes to Consolidated Financial Statements for a discussion of recent accounting pronouncements.

Table of ContentsContractual Obligations

The following table summarizes our contractual obligations as of December 31, 2014, (\$000s):

Contractual Obligations	Total	Payments Due by Period					
		2015	2016	2017	2018	2019	Thereafter
Long-term debt(1)	\$ 895,238	\$	\$	\$ 90,563	\$ 573,563	\$	\$ 231,112
Receivable credit facility(1)	167,000				167,000		
Interest on long-term debt(2)	83,679	21,156	21,208	20,643	12,738	5,163	2,771
Operating lease obligations(3)	89,227	12,219	15,708	13,365	8,273	7,463	32,199
Purchase obligations(4)	201,552	36,063	31,289	28,183	24,097	19,665	62,255
Minimum pension plan funding(5)	1,108	1,108					
<b>Total</b>	<b>\$ 1,437,804</b>	<b>\$ 70,546</b>	<b>\$ 68,205</b>	<b>\$ 152,754</b>	<b>\$ 785,671</b>	<b>\$ 32,291</b>	<b>\$ 328,337</b>

- 
- (1) These obligations are reflected on our Consolidated Balance Sheets at December 31, 2014, in long-term debt net of current portion, as appropriate. See Note 9 "Pension and Postretirement Benefits" in the Notes to Consolidated Financial Statements.
- (2) Assumes debt is carried to full term. Debt bears interest at variable rates and the amounts above assume future interest will be incurred at the rates in effect on December 31, 2014. These obligations are not reflected on our Consolidated Balance Sheets at December 31, 2014.
- (3) These obligations are not reflected on our Consolidated Balance Sheet at December 31, 2014. See Note 13 in the Notes to Consolidated Financial Statements.
- (4) Purchase obligations are agreements to purchase goods that are enforceable and legally binding on us and that specify all significant terms, including fixed or minimum quantities to be purchased. These obligations are not reflected on our Consolidated Balance Sheets at December 31, 2014. See Note 13 in the Notes to Consolidated Financial Statements regarding the Company's purchase obligation relating to the Long Term Fiber Supply with MWV/Plum Creek.
- (5) The Company's defined benefit retirement plans requires a minimum pension plan contribution of approximately \$1.1 million in 2015 and was determined in consultation with our actuary in accordance with ERISA guidelines. See Note 9 in the Notes to Consolidated Financial Statements.

**Item 7A. Quantitative and Qualitative Disclosures about Market Risk**

Market risk is the sensitivity of income to changes in interest rates, commodity prices and foreign currency changes. The Company is exposed to the following types of market risk: interest rates, commodity prices and foreign currency.

Interest Rates

Under our Amended and Restated Credit Agreement, at December 31, 2014 we had an outstanding Credit Facility consisting of two term loans totaling approximately \$895.2 million and the Revolver totaling \$400 million. Depending on the type of borrowing, the applicable interest rate under the Credit Facility is calculated at a per annum rate equal to (a) LIBOR plus an applicable margin or (b) the base rate that is calculated as (i) the greatest of (x) the prime rate, (y) the federal funds effective rate plus 0.50% or (z) a daily rate equal to one month LIBOR plus 1% plus (ii) an applicable margin. The unused portion of the Revolver is also subject to an unused fee that is calculated at a per annum rate (the "Unused



Fee Rate").

The applicable margin for borrowings under the Credit Facility and the Unused Fee Rate will be determined by reference to the pricing grid based on the Company's total leverage ratio. Under such

Table of Contents

pricing grid, the applicable margins for Term Loan A-1 and Revolver ranges from 1.0% to 2.0% for Eurodollar loans and from 0.0% to 1.0% for base rate loans and the Unused Fee Rate ranges from 0.25% to 0.40%. The applicable margins for Term Loan A-2 ranges from 1.25% to 2.25% for Eurodollar loans and from 0.25% to 1.25% for base rate loans. At December 31, 2014 the weighted average interest rate of the term loans was 1.98 percent.

Under our Receivables Credit Facility, at December 31, 2014 we have \$167.0 million outstanding. The outstanding capital of each investment in the Receivables interests shall accrue yield for each day at a rate per annum equal to the sum of (a) for any day, the one-month Eurodollar rate for U.S. dollar deposits plus (b) the applicable margin. At December 31, 2014 the interest rate of the Receivables Credit Facility was 0.9 percent.

Changes in market rates may impact the base or LIBOR rate under all borrowings. For instance, if the bank's LIBOR rate was to increase or decrease by one percentage point (1.0%), our annual interest expense would change by approximately \$10.8 million based upon our expected future monthly term loan balances per our existing repayment schedule.

Commodity Prices

We are exposed to price fluctuations of certain commodities used in production. Key materials and energy used in the production process include roundwood and woodchips, recycled fiber (OCC), containerboard, fuel oil, natural gas, electricity and caustic soda. We generally purchase these materials and energy at market prices, and do not use forward contracts or other financial instruments to hedge our exposure to price risk related to these commodities. We have one contract to purchase coal at fixed prices through December 31, 2015.

We are exposed to price fluctuations in the price of our finished goods. The prices we charge for our products are primarily based on market conditions.

Foreign Currency

We are exposed to currency fluctuations as we invoice certain European customers in Euros. As of December 31, 2014 and 2013 the Company did not have any foreign currency forward contracts and foreign exchange forward contracts outstanding.

As of December 31, 2014, trade accounts receivable denominated in Euros totaled \$5.8 million.

**Item 8. Financial Statements and Supplementary Data**

Financial statements are attached hereto beginning on Page F-1.

**Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure**

None.

**Item 9A. Controls and Procedures**

Disclosure Controls and Procedures.

An evaluation of the effectiveness of our disclosure controls and procedures as of December 31, 2014 was made by our Chief Executive Officer and Chief Financial Officer. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of the end of the period covered by this report.

Table of Contents

**Internal Control over Financial Reporting.**

*Management Annual Report on Internal Control over Financial Reporting.* Our management's report on internal control over financial reporting is set forth on page F-2 of this report.

*Changes in Internal Control over Financial Reporting.* There were no changes in our internal control over financial reporting during the most recent fiscal quarter that have materially affected, or are reasonably likely to affect, our internal control over financial reporting.

**Item 9B. Other Information**

None.

**PART III**

**Item 10. Directors, Executive Officers and Corporate Governance**

The information required by this item is incorporated by reference from our definitive proxy statement to be filed on or about March 31, 2015 with the Securities and Exchange Commission ("SEC").

Additional information required by this Item (i) with respect to members of our Board of Directors will be contained in the Company's Proxy Statement to be filed with the SEC on or about March 31, 2015 under the caption "Proposal 1 Election of Directors," (ii) with respect to our executive officers will be contained in the Company's Proxy Statement under the caption "Executive Officers," (iii) with respect to our audit committee will be contained in the Company's Proxy Statement under the caption "Governance Structure What Committees has the Board Established?," (iv) with respect to compliance under Section 16(a) of the Securities Exchange Act of 1934 will be contained in Company's Proxy Statement under the caption "Section 16(a) Beneficial Ownership Reporting Compliance," and (v) with respect to our code of ethics will be contained in the Company's Proxy Statement under the caption "Code of Ethics," and is incorporated herein by this reference.

KapStone adopted a code of ethics that applies to its CEO and CFO, as well as all other officers and employees of the Company and its affiliates. This code of ethics, entitled "Code of Conduct and Ethics", is posted on the Company's website at [www.kapstonepaper.com](http://www.kapstonepaper.com) under "Governance." The Code of Conduct and Ethics is administered by the Chief Compliance Officer of the Company. Any amendment to, or waiver of, a provision of the code of ethics that applies to the CEO, CFO, or persons performing similar functions will be disclosed on the Company's website under "Governance." We will also provide a copy of the Code of Conduct and Ethics without charge at the written request of any shareholder of record. Requests for copies may be directed to the Chief Compliance Office at our corporate headquarters.

**Item 11. Executive Compensation**

The information required by this Item will be contained in the Company's Proxy Statement to be filed with the SEC on or about March 31, 2015 under the captions "Executive Compensation," "Summary Compensation Table," "Grants of Plan-Based Awards," "Governance Structure," "Outstanding Equity Awards at 2014 Fiscal Year End," "Potential Payments upon Termination or Change-in-Control," and "2014 Director Compensation" and is incorporated herein by this reference.

**Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters**

The information required by this Item will be contained in the Company's Proxy Statement to be filed with the SEC on or about March 31, 2015 under the captions "Stock Ownership Securities

Table of Contents

Authorized for Issuance Under Equity Compensation Plan", "Stock Ownership Security Ownership of Management" and "Stock Ownership Security Ownership of Certain Beneficial Stockholders" and is incorporated herein by this reference.

**Item 13. Certain Relationships and Related Persons Transactions and Director Independence**

The information required by this Item will be contained in the Company's Proxy Statement to be filed with the SEC on or about March 31, 2015 under the captions "Certain Relationships and Related Person Transactions," and "Governance Structure" is incorporated herein by this reference.

**Item 14. Principal Accountant Fees and Services**

The information required by this Item will be contained in the Company's Proxy Statement to be filed with the SEC on or about March 31, 2015 under the caption "Independent Registered Public Accounting Firm" and is incorporated herein by this reference.

**PART IV**

**Item 15. Exhibits and Financial Statement Schedules**

(a)

(1) *Financial Statements*

An index to Consolidated Financial Statements appears on page F-1.

(a)

(2) *Financial Statement Schedules*

Certain financial statement schedules have been omitted because they are not applicable or the required information is shown in the financial statements or the notes thereto.

(b)

*Exhibits.*

The following Exhibits are filed as part of this report:

<b>Exhibit No.</b>	<b>Description</b>
2.1	Agreement and Plan of Merger, dated as of September 22, 2011, by and among KapStone Kraft Paper Corporation, U.S. Corrugated Acquisition Inc., Pine Merger Corp., Dennis Dorian Mehiel, for purposes of Section 10.3, and Dennis Mehiel, for purposes of Section 10.3 and as the Representative. Incorporated by reference to the Registrant's Current Report on Form 8-K filed on September 22, 2011.
2.2	Stock Purchase Agreement dated as of June 10, 2013, by and among KapStone Kraft Paper Corporation, Longview Fibre Paper and Packaging, Inc., Brookfield Capital Partners II (NR) L.P., Brookfield Capital Partners II (PC) L.P., Brookfield Capital Partners II L.P. and KapStone Paper and Packaging Corporation. Incorporated by reference to the Registrant's Current Report on Form 8-K filed on June 10, 2013.
3.1	Restated Certificate of Incorporation of KapStone Paper and Packaging Corporation (as amended through January 2, 2007). Incorporated by reference to the Registrant's Annual Report on Form 10-K for the period ended December 31, 2009, filed on March 10, 2010.
3.2	Amended and Restated By-laws. Incorporated by reference to the Registrant's Current Report on Form 8-K filed on May 19, 2014.
4.1	Specimen Common Stock Certificate. Incorporated by reference to the Registrant's Registration Statement on Form S-1/A (File No. 333-124601) filed on June 14, 2005.



## Edgar Filing: KAPSTONE PAPER & PACKAGING CORP - Form 10-K

### Table of Contents

<b>Exhibit No.</b>	<b>Description</b>
10.1*	2006 Incentive Plan amended and restated as of May 18, 2012. Incorporated by reference to the Registrant's Annual Report filed on Form 10-K filed on March 4, 2013.
10.2*	Performance Incentive Plan of KapStone Paper and Packaging Corporation. Incorporated by reference to the Registrant's Current Report on Form 8-K filed on April 14, 2008.
10.3*	Form of Restricted Stock Unit Agreement. Incorporated by reference to the Registrant's Current Report on Form 8-K filed on April 14, 2008.
10.4*	Restricted Stock Unit Agreement Amendment November 28, 2012 issued on or about May 27, 2012 between KapStone Paper and Packaging Corporation and Grantee. Incorporated by reference to the Registrant's Form 10-K filed on March 4, 2013.
10.5*	2014 Incentive Plan. Incorporated by reference to Annex A to Registrant's Definitive Proxy Statement filed on April 1, 2014.
10.6*	KapStone Paper and Packaging Corporation Deferred Compensation Plan and the Adoption Agreement for the KapStone Paper and Packaging Corporation Deferred Compensation Plan. Incorporated by reference to the Registrant's Current Report on Form 8-K filed on December 16, 2014.
10.7	Long-Term Fiber Supply Agreement, dated July 1, 2008, by and among MeadWestvaco Forestry LLC and KapStone Charleston Kraft LLC (with certain confidential information deleted there from). Incorporated by reference to the Registrant's Current Report on Form 8-K filed on July 2, 2008.
10.8	Amended and Restated Credit Agreement dated as of July 18, 2013, by and among KapStone Paper and Packaging Corporation, KapStone Kraft Paper Corporation, as Borrower, the subsidiaries of Borrower named therein, as Guarantors, the lenders named therein, Bank of America, N.A., as Administrative Agent, Swing Line Lender and L/C Issuer, and Barclays Bank PLC and Wells Fargo Bank, National Association, as co-Syndication Agents. Incorporated by reference to the Registrant's Form 8-K filed on July 18, 2013.
10.9	First Amendment to Amended and Restated Credit Agreement, dated as of April 2, 2014, by and among KapStone Kraft Paper Corporation, as Borrower, KapStone Paper and Packaging Corporation and the other Guarantors party thereto, the Lenders party thereto and Bank of America N.A., as Administrative Agent, Swing Line Lender and L/C Issuer. Incorporated by reference to the Registrant's Form 8-K filed on April 4, 2014.
10.10	Second Amendment to Amended and Restated Credit Agreement dated as of August 15, 2014, by and among KapStone Paper and Packaging Corporation, KapStone Kraft Paper Corporation, as Borrower, the subsidiaries of KapStone Paper and Packaging Corporation named therein, as Guarantors, the lenders named therein and Bank of America, N.A., as Administrative Agent, Swing Line Lender and L/C Issuer. Incorporated by reference to the Registrant's Form 10-Q filed on October 29, 2014.
10.11	Third Amendment to Amended and Restated Credit Agreement dated as of December 16, 2014, by and among KapStone Paper and Packaging Corporation, KapStone Kraft Paper Corporation, as Borrower, the subsidiaries of KapStone Paper and Packaging Corporation named therein, as Guarantors, the lenders named therein and Bank of America, N.A., as Administrative Agent, Swing Line Lender and L/C Issuer.

## Edgar Filing: KAPSTONE PAPER & PACKAGING CORP - Form 10-K

### Table of Contents

<b>Exhibit No.</b>	<b>Description</b>
10.12	Receivables Purchase Agreement, dated as of September 26, 2014, by and among KapStone Paper and Packaging Corporation, as Servicer, KapStone Receivables, LLC, as Seller, the financial institutions from time to time party thereto, as Purchasers, and Wells Fargo Bank, N.A., as Administrative Agent. Incorporated by reference to the Registrant's Form 8-K filed on October 1, 2014.
10.13	Receivables Sale Agreement, dated as of September 26, 2014, by and among KapStone Paper and Packaging Corporation, as Servicer, KapStone Receivables, LLC, as Buyer, and KapStone Kraft Paper Corporation, KapStone Container Corporation, KapStone Charleston LLC and Longview Fibre Paper and Packaging, Inc., as Originators. Incorporated by reference to the Registrant's Form 8-K filed on October 1, 2014.
14.0	Code of Ethics. Incorporated by reference to the Registrant's Annual Report filed on Form 10-K filed on March 4, 2013.
21.1	Subsidiaries.
23.1	Consent of Ernst & Young LLP.
31.1	Certification of the Chief Executive Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act, as amended.
31.2	Certification of the Principal Financial Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act, as amended.
32.1	Certification of the Chief Executive Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification of the Principal Financial Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	XBRL Instance Document.
101.SCH	XBRL Taxonomy Extension Schema.
101.CAL	XBRL Taxonomy Extension Calculation Linkbase.
101.DEF	XBRL Taxonomy Extension Definition Linkbase.
101.LAB	XBRL Taxonomy Extension Label Linkbase.
101.PRE	XBRL Extension Presentation Linkbase.

---

\*

Management compensatory plan or arrangement.







Table of Contents

**KapStone Paper and Packaging Corporation**  
**(INDEX TO FINANCIAL STATEMENTS)**

<b>Financial Statements</b>	<b>Page</b>
<u>Management's Annual Report on Internal Control over Financial Reporting</u>	<u>F-2</u>
<u>Report of Independent Registered Public Accounting Firm on Internal Control over Financial Reporting</u>	<u>F-3</u>
<u>Report of Independent Registered Public Accounting Firm for 2014, 2013, and 2012</u>	<u>F-4</u>
<u>Consolidated Balance Sheets as of December 31, 2014, and December 31, 2013</u>	<u>F-5</u>
<u>Consolidated Statements of Comprehensive Income for the years ended December 31, 2014, 2013, and 2012</u>	<u>F-6</u>
<u>Consolidated Statements of Changes in Stockholders' Equity for the years ended December 31, 2014, 2013 and 2012</u>	<u>F-7</u>
<u>Consolidated Statements of Cash Flows for years ended December 31, 2014, 2013, and 2012</u>	<u>F-8</u>
<u>Notes to Consolidated Financial Statements</u>	<u>F-9</u>

F-1

---

Table of Contents

**MANAGEMENT'S ANNUAL REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING**

Our management is responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting is defined in Rule 3a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934. Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements and can provide only reasonable assurance with respect to financial statement preparation and presentation. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Management assessed the effectiveness of our internal control over financial reporting as of December 31, 2014. Management based this assessment on the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in "*Internal Control Integrated Framework* (2013 Framework)."

Based on this assessment, management concluded that, as of December 31, 2014, our internal control over financial reporting is effective.

Ernst & Young LLP, an independent registered public accounting firm, has audited the consolidated financial statements of the Company and the Company's internal control over financial reporting and has included their reports herein.

Table of Contents

**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

Board of Directors and Stockholders  
KapStone Paper and Packaging Corporation

We have audited KapStone Paper and Packaging Corporation's internal control over financial reporting as of December 31, 2014, based on criteria established in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 Framework) (the COSO criteria). KapStone Paper and Packaging Corporation'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 Annual 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 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 its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that 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, KapStone Paper and Packaging Corporation maintained, in all material respects, effective internal control over financial reporting as of December 31, 2014, based on the COSO criteria.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of KapStone Paper and Packaging Corporation as of December 31, 2014 and 2013, and the related statements of comprehensive income, changes in stockholders' equity, and cash flows for each of the three years in the period ended December 31, 2014, and our report dated February 27, 2015, expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP

Chicago, Illinois  
February 27, 2015

Table of Contents

**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

Board of Directors and Stockholders  
KapStone Paper and Packaging Corporation

We have audited the accompanying consolidated balance sheets of KapStone Paper and Packaging Corporation as of December 31, 2014 and 2013, and the related consolidated statements of comprehensive income, changes in stockholders' equity and cash flows for each of the three years in the period ended December 31, 2014. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements 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, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of KapStone Paper and Packaging Corporation as of December 31, 2014 and 2013, and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 2014, in conformity with U.S. generally accepted accounting principles.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), KapStone Paper and Packaging Corporation's internal control over financial reporting as of December 31, 2014, based on criteria establish in Internal Control Integrated Framework, issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 Framework) and our report dated February 27, 2015 expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP

Chicago, Illinois  
February 27, 2015

Table of Contents**KapStone Paper and Packaging Corporation****Consolidated Balance Sheets****(In thousands, except share and per share amounts)**

	<b>December 31,</b>	
	<b>2014</b>	<b>2013</b>
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 28,467	\$ 12,967
Trade accounts receivable (Includes \$225,577 at December 31, 2014, associated with the securitization facility)	228,740	232,347
Other receivables	12,833	11,399
Inventories	238,329	217,382
Prepaid expenses and other current assets	7,172	6,405
<b>Total current assets</b>	<b>515,541</b>	<b>480,500</b>
Plant, property and equipment, net	1,386,670	1,389,609
Other assets	10,135	129,493
Intangible assets, net	110,077	123,745
Goodwill	533,851	528,515
<b>Total assets</b>	<b>\$ 2,556,274</b>	<b>\$ 2,651,862</b>
<b>Liabilities and Stockholders' Equity</b>		
Current liabilities:		
Current portion of long-term debt	\$	\$ 4,950
Dividend payable	9,911	223
Accounts payable	149,600	159,127
Accrued expenses	48,340	45,662
Accrued compensation costs	62,491	54,871
Accrued income taxes	6,477	
Deferred income taxes	1,990	5,445
<b>Total current liabilities</b>	<b>278,809</b>	<b>270,278</b>
Other liabilities:		
Long-term debt, net of current portion (Includes \$167,000 at December 31, 2014, associated with the securitization facility)	1,046,063	1,192,413
Pension and postretirement benefits	32,800	69,611
Deferred income taxes	412,293	444,672
Other liabilities	8,182	8,808
<b>Total other liabilities</b>	<b>1,499,338</b>	<b>1,715,504</b>
Stockholders' equity:		
Preferred stock \$0.0001 par value; 1,000,000 shares authorized; no shares issued and outstanding		
Common stock \$0.0001 par value; 175,000,000 shares authorized; 96,046,554 shares issued and outstanding (excluding 40,000 treasury shares) at December 31, 2014 and 95,666,212 shares issued and outstanding (excluding 40,000 treasury shares) at December 31, 2013	10	10

Edgar Filing: KAPSTONE PAPER & PACKAGING CORP - Form 10-K

Additional paid-in-capital	255,505	246,186
Retained earnings	574,601	412,349
Accumulated other comprehensive income / (loss)	(51,989)	7,535
Total stockholders' equity	778,127	666,080
Total liabilities and stockholders' equity	\$ 2,556,274	\$ 2,651,862

See notes to consolidated financial statements.

F-5

---

Table of Contents**KapStone Paper and Packaging Corporation****Consolidated Statements of Comprehensive Income****(In thousands, except share and per share amounts)**

	Years Ended December 31,		
	2014	2013	2012
Net sales	\$ 2,300,920	\$ 1,748,162	\$ 1,216,637
Cost of sales, excluding depreciation and amortization	1,551,531	1,186,930	866,124
Depreciation and amortization	136,548	95,435	63,124
Freight and distribution expenses	175,901	135,972	108,438
Selling, general, and administrative expenses	137,009	110,612	70,055
Other operating income		675	664
<b>Operating income</b>	<b>299,931</b>	<b>219,888</b>	<b>109,560</b>
Foreign exchange (gain)/loss	1,222	(232)	303
Loss on debt extinguishment	5,617		
Interest expense, net	32,491	25,130	11,774
<b>Income before provision for income taxes</b>	<b>260,601</b>	<b>194,990</b>	<b>97,483</b>
Provision for income taxes	88,686	67,652	34,978
<b>Net income</b>	<b>\$ 171,915</b>	<b>\$ 127,338</b>	<b>\$ 62,505</b>
<b>Other comprehensive income, net of tax</b>			
Defined pension and post-retirement plans:			
Net actuarial gain/(loss)	(59,645)	10,491	(909)
Pension and postretirement plan reclassification adjustments:			
Amortization (accretion) of prior service costs	128	(43)	105
Amortization (accretion) of net gain / loss	(7)	189	162
<b>Other comprehensive income/(loss), net of tax</b>	<b>(59,524)</b>	<b>10,637</b>	<b>(642)</b>
<b>Total comprehensive income</b>	<b>\$ 112,391</b>	<b>\$ 137,975</b>	<b>\$ 61,863</b>
<b>Weighted average number of shares outstanding:</b>			
Basic	95,900,179	95,258,756	93,426,912
Diluted	97,459,184	96,739,482	95,452,878
<b>Net income per share:</b>			
Basic	\$ 1.79	\$ 1.34	\$ 0.67



Edgar Filing: KAPSTONE PAPER & PACKAGING CORP - Form 10-K

Diluted	\$	1.76	\$	1.32	\$	0.65
---------	----	------	----	------	----	------

Dividends declared per common share	\$	0.10	\$		\$	1.00
-------------------------------------	----	------	----	--	----	------

See notes to consolidated financial statements.

F-6

---

Table of Contents**KapStone Paper and Packaging Corporation****Consolidated Statements of Changes in Stockholders' Equity****(In thousands, except share amounts)**

	Common Stock, net of Treasury Stock		Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Stockholders' Equity
	Shares	Amount				
<b>Balance December 31, 2011</b>	92,899,390	\$ 10	\$ 230,660	\$ 318,068	\$ (2,460)	\$ 546,278
Stock-based compensation expense			5,242			5,242
Payment of withholding taxes on vested restricted stock awards and options exercised	404,168		(9,496)			(9,496)
Exercise of stock options	1,574,454		1,345			1,345
Excess tax benefit from stock-based compensation			8,037			8,037
Employee Stock Purchase Plan	32,108		241			241
Special Cash Dividend				(95,562)		(95,562)
Net income				62,505		62,505
Pension and postretirement plan adjustments, net of tax of \$386					(642)	(642)
<b>Balance December 31, 2012</b>	94,910,120	\$ 10	\$ 236,029	\$ 285,011	\$ (3,102)	\$ 517,948
Stock-based compensation expense			5,203			5,203
Payment of withholding taxes on vested restricted stock awards and options exercised	127,952		(860)			(860)
Exercise of stock options	602,900		1,934			1,934
Excess tax benefit from stock-based compensation			3,531			3,531
Employee Stock Purchase Plan	25,240		349			349
Net income				127,338		127,338
Pension and postretirement plan adjustments, net of tax of \$6,281					10,637	10,637
<b>Balance December 31, 2013</b>	95,666,212	\$ 10	\$ 246,186	\$ 412,349	\$ 7,535	\$ 666,080
Stock-based compensation expense			6,956			6,956
Payment of withholding taxes on vested restricted stock awards and options exercised	176,724		(1,755)			(1,755)
Exercise of stock options	183,130		869			869
Excess tax benefit from stock-based compensation			2,649			2,649
Employee Stock Purchase Plan	20,488		600			600
Dividends declared				(9,663)		(9,663)
Net income				171,915		171,915
Pension and postretirement plan adjustments, net of tax of \$34,346					(59,524)	(59,524)

<b>Balance December 31, 2014</b>	96,046,554	\$	10	\$	255,505	\$	574,601	\$	(51,989)	\$	778,127
----------------------------------	------------	----	----	----	---------	----	---------	----	----------	----	---------

See notes to consolidated financial statements.

F-7

---

Table of Contents**KapStone Paper and Packaging Corporation****Consolidated Statements of Cash Flows****(In thousands)**

	<b>Years Ended December 31,</b>		
	<b>2014</b>	<b>2013</b>	<b>2012</b>
<b>Operating activities</b>			
Net income	\$ 171,915	\$ 127,338	\$ 62,505
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	136,548	95,435	63,124
Stock-based compensation expense	6,956	5,203	5,242
Pension and postretirement	(11,523)	(3,908)	1,489
Excess tax benefit from stock-based compensation	(2,649)	(3,531)	(8,037)
Amortization of debt issuance costs	5,696	4,489	3,479
Loss on debt extinguishment	5,617		
Loss on disposal of fixed assets	4,252	1,012	1,202
Deferred income taxes	2,455	59,865	23,128
Changes in assets and liabilities:			
Trade accounts receivable, net	3,649	(11,133)	(1,796)
Other receivables	(1,434)	6,374	1,186
Inventories	(22,973)	2,934	(1,248)
Prepaid expenses and other current assets	(767)	9,488	(5,601)
Other assets	(1,433)	(382)	(452)
Accounts payable	(5,705)	(6,191)	9,163
Accrued expenses and other liabilities	6,072	(3,364)	10,572
Accrued compensation costs	7,620	15,065	(6,127)
Accrued income taxes	8,902		
 Net cash provided by operating activities	 313,198	 298,694	 157,829
<b>Investing activities</b>			
Longview acquisition, net of cash acquired		(538,239)	
USC acquisition, net of cash acquired			(314)
Capital expenditures	(137,232)	(96,706)	(67,237)
 Net cash used in investing activities	 (137,232)	 (634,945)	 (67,551)
<b>Financing activities</b>			
Proceeds from revolving credit facility	97,900	321,613	142,900
Repayments on revolving credit facility	(97,900)	(385,113)	(79,400)
Proceeds from receivables credit facility	175,000		
Repayments on receivables credit facility	(8,000)		
Proceeds from long-term debt		1,275,000	
Repayments of long-term debt	(328,525)	(356,550)	(50,000)
Redemption of Longview senior notes		(507,520)	
Special cash dividend	(223)		(94,910)
Payment of loan amendment and debt issuance costs	(1,081)	(19,654)	(569)
Proceeds from other current borrowings	6,300	5,115	3,398
Repayments on other current borrowings	(6,300)	(5,115)	(3,398)
Payment of withholding taxes on stock awards	(1,755)	(860)	(9,496)
Proceeds from exercises of stock options	869	1,934	1,345
Proceeds from shares issued to ESPP	600	349	241
Excess tax benefit from stock-based compensation	2,649	3,531	8,037

Edgar Filing: KAPSTONE PAPER & PACKAGING CORP - Form 10-K

Net cash provided by (used in) financing activities	(160,466)	332,730	(81,852)
Net increase (decrease) in cash and cash equivalents	15,500	(3,521)	8,426
Change in cash equivalents-beginning of period	12,967	16,488	8,062
Change in cash equivalents-end of period	\$ 28,467	\$ 12,967	\$ 16,488

See notes to consolidated financial statements.

F-8

---

Table of Contents

**KAPSTONE PAPER AND PACKAGING CORPORATION**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**(\$ in thousands, except share and per share amounts)**

**1. Description of Business and Basis of Presentation**

KapStone Paper and Packaging Corporation, or the "Company," operates as one segment, produces and sells a variety of containerboard, corrugated products and specialty paper products in the United States and globally. The Company was incorporated on April 15, 2005 in Delaware.

On July 18, 2013, the Company acquired 100 percent of the stock of Longview Fibre Paper and Packaging, Inc. ("Longview"). As a result of the Longview acquisition, the accompanying consolidated financial statements are not comparative. The accompanying consolidated financial statements include the results of Longview since July 18, 2013 (see Note 3 "Longview Acquisition").

**Principles of Consolidation** The consolidated financial statements have been prepared on the accrual basis of accounting in conformity with accounting principles generally accepted in the United States of America ("U.S. GAAP"). The consolidated financial statements include the accounts of the Company and its subsidiaries. All significant intercompany accounts and transactions have been eliminated. In the opinion of management, all adjustments (consisting of a normal recurring nature) considered necessary for a fair presentation have been included. The Consolidated Financial Statements also include the results of companies acquired by the Company from the date of each acquisition.

**Use of Estimates** The preparation of financial statements and related disclosures requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. The Company bases its estimates on historical experience and on other assumptions that its management believes are reasonable under the circumstances. These estimates form the basis for making judgments about the carrying value of asset and liabilities when those values are not readily apparent from other sources. Actual results could materially differ from these estimates.

**2. Significant Accounting Policies**

**Revenue Recognition** Revenue is recognized when the customer takes title and assumes the risks and rewards of ownership, when the price is fixed and determinable and when collectability is reasonably assured. Sales with terms f.o.b. (free on board) shipping point are recognized at the time of shipment. For sales transactions with terms f.o.b. destination, revenue is recorded when the product is delivered to the customer's site and when title and risk of loss are transferred. Sales on consignment are recognized in revenue at the earlier of the month that the goods are consumed or after a period of time subsequent to receipt by the customer as specified by contract terms, provided all other revenue recognition criteria is met. Incentive rebates are typically paid in cash and are netted against revenue on an accrual basis as qualifying purchases are made by the customer to earn and thereby retain the rebate.

Freight charged to customers is recognized in net sales.

**Cost of Sales** Cost of sales includes material, labor and overhead costs, but excludes depreciation and amortization. Proceeds received from the sale of by-products generated from the paper and packaging manufacturing process are reflected as a reduction to cost of sales. Income from sales of by-products is derived primarily from the sale of tall oil, hardwood, turpentine and waste bales to third parties. During 2014, 2013 and 2012, cost of sales was reduced by \$35.8 million, \$32.3 million and \$23.0 million, respectively for these by-product sales.

Table of Contents

## KAPSTONE PAPER AND PACKAGING CORPORATION

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(\$ in thousands, except share and per share amounts)

**2. Significant Accounting Policies (Continued)**

**Freight and distribution expenses** Freight and distribution include shipping and handling costs for product sold to customers and is excluded from cost of sales.

**Planned Maintenance Outage Costs** The Company recognizes the cost of maintenance activities in the period in which they occur under the direct expense method in accordance with ASC 360, *Property, Plant and Equipment*. The Company performs annual planned maintenance outages at its Roanoke Rapids, Longview and Cowpens mills. Costs of approximately \$36.1 million, \$24.9 million and \$18.4 million related to planned maintenance outages are included in cost of sales for the years ended December 31, 2014, 2013 and 2012, respectively.

**Net Income per Common Share** Basic net income per share is based on the weighted average number of common shares outstanding during the period. Diluted income per share reflects the potential dilution assuming common shares were issued for the exercise of outstanding in-the-money stock options and unvested restricted stock awards and assuming the proceeds thereof were used to purchase common shares at the average market price during the period such awards were outstanding and inclusion of such shares is dilutive to net income per share.

**Concentrations of Risk** Financial instruments that potentially expose the Company to concentrations of credit and market risk consist primarily of cash and cash equivalents and trade accounts receivable from sales of product to third parties. When excess cash and cash equivalents are invested they are placed in investment grade commercial paper.

No customer accounted for more than 10 percent of consolidated net sales in 2014, 2013 and 2012. In order to mitigate credit risk, the Company obtains letters of credit for certain export customers. For the years ended December 31, 2014, 2013 and 2012, net sales to US based customers were 80 percent, 80 percent and 77 percent, respectively, of consolidated net sales. Net sales to foreign based customers during 2014, 2013 and 2012 were 20 percent, 20 percent and 23 percent, respectively, of consolidated net sales. See Note 15 "Segment Information".

The Company establishes its allowance for doubtful accounts based upon factors mainly surrounding the credit risks of specific customers and other related information. Once an account is deemed uncollectible, it is written off. At December 31, 2014, 2013 and 2012 changes to the allowance for doubtful accounts are summarized as follows (\$000's):

Year ended:	Balance at beginning of year	Charged to Expense	Deductions	Balance at end of year
December 31, 2014(1)	\$ 682	\$ 217	\$ (614)	\$ 285
December 31, 2013	\$ 96	\$ 607	\$ (21)	\$ 682
December 31, 2012(2)	\$ 571	\$ 97	\$ (572)	\$ 96

(1) Deductions in 2014 include \$0.6 million of accounts written-off.

(2) Deductions in 2012 include a \$0.4 million valuation adjustment and \$0.2 million of accounts written-off.

Table of Contents

## KAPSTONE PAPER AND PACKAGING CORPORATION

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(\$ in thousands, except share and per share amounts)

**2. Significant Accounting Policies (Continued)**

**Foreign Currency Transactions** The Company invoices certain European customers in Euros. Trade accounts receivable denominated in euros are remeasured into U.S. dollars at the year-end rate of exchange and statements of comprehensive income items are translated at the weighted average exchange rates for the period. Gains and losses arising from these transactions are included in foreign exchange (gain) / loss within the Consolidated Statements of Comprehensive Income.

**Cash and Cash Equivalents** Cash equivalents include all highly liquid investments with maturities of three months or less when purchased.

**Fair value of Financial Instruments** The Company's cash and cash equivalents, trade accounts receivables and accounts payables are financial assets and liabilities with carrying values that approximate fair value. The Company's variable rate term loans and short-term borrowing are financial liabilities with fair values that approximate their carrying value of \$1.1 billion. See Note 8 "*Long-term debt*".

**Inventories** Inventories are valued at the lower of cost or market; whereby cost includes all direct and indirect materials, labor and manufacturing overhead, less by-product recoveries. Costs of raw materials, work-in-process, and finished goods are determined using the first-in, first-out method for the legacy KapStone locations. Replacement parts and other supplies are stated using the average cost method. Purchases and sales of inventory with the same counterparty that are entered into in contemplation of one another are combined and recorded as exchanges of inventory measured at the book value of the item exchanged.

In conjunction with the Longview acquisition, KapStone acquired Longview's inventories which were stated at fair value. Cost for the Longview inventories is determined on a last-in, first-out method except for replacement parts and supplies inventories, which are valued using the average cost method.

**Plant, Property, and Equipment, net** Plant, property, and equipment are stated at cost less accumulated depreciation. Property, plant, and equipment acquired in acquisitions were recorded at fair value on the date of acquisition. Depreciation is computed using the straight-line method over the assets' estimated useful lives. The range of estimated useful lives is as follows:

	Years
Land improvements	3 - 25
Buildings	11 - 40
Machinery and equipment	3 - 30
Furniture and office equipment	5 - 10
Computer hardware and software	3 - 5

The Company accounts for costs incurred for the development of software for internal use in accordance with ASC 350

*Intangibles Goodwill and Other*. This standard requires the capitalization of certain costs incurred in connection with developing or obtaining internal use software.

**Goodwill and Intangible Assets** Goodwill is the excess of purchase price over the fair value of the net assets of businesses acquired. On an annual basis and in accordance with ASC 350, *Intangibles Goodwill and Other*, the Company evaluates goodwill for impairment using a qualitative assessment to



Table of Contents

**KAPSTONE PAPER AND PACKAGING CORPORATION**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**(\$ in thousands, except share and per share amounts)**

**2. Significant Accounting Policies (Continued)**

determine whether it is more likely than not that fair value of any reporting unit is less than its carrying amount. If the Company determines that the fair value of the reporting unit may be less than its carrying amount, the Company evaluates goodwill using a two-step quantitative impairment test. Otherwise, the Company concludes that no impairment is indicated and does not perform the two-step quantitative impairment test.

If the qualitative assessment concludes that the two-step impairment test is necessary, the first step is to compare the book value of the reporting unit, including goodwill, with its fair value. A reporting unit is an operating segment or one level below an operating segment (referred to as a "component"). A component is considered a reporting unit for purposes of goodwill testing if the component constitutes a business for which discrete financial information is available and segment management regularly reviews the operating results of that component. The Company has identified three reporting units. The fair value is estimated based on a market approach and a discounted cash flow analysis, also known as the income approach, and is reconciled back to the current market capitalization for the Company to ensure that the implied control premium is reasonable. A discounted cash flow analysis requires the Company to make various judgmental assumptions, including assumptions about future cash flows, growth rates and discount rates. The assumptions about future cash flows and growth rates are based on the forecast and long-term business plans of each reporting unit. Discount rate assumptions are considered Level 3 inputs in the fair value hierarchy defined in ASC 820, *Fair Value Measurements and Discounts*. Management also considers market-multiple information to corroborate the fair value conclusions reached using the discounted cash flow analysis. If necessary, the second step of the goodwill impairment test compares the implied fair value of the reporting unit's goodwill with the carrying amount of that goodwill. The implied fair value of goodwill is determined in the same manner as the amount of goodwill recognized in a business combination. The Company's goodwill impairment analysis is performed annually at the beginning of the fourth quarter or more frequently if there is an indicator of impairment and did not result in an impairment charge for any periods presented.

Intangible assets acquired in a business combination or asset purchase are initially valued at the fair market value using generally accepted valuation methods appropriate for the type of the intangible asset. Definite-lived intangible assets are amortized over their estimated useful lives and are reviewed for impairment if indicators of impairment arise. The evaluation of the impairment is based upon a comparison of the carrying amount of the intangible asset to the estimated future undiscounted cash flows expected to be generated by the asset. If the estimated undiscounted future cash flows are less than the carrying amount of the assets, the asset is considered to be impaired. If impaired, the intangible asset is written down to estimated fair market value.

**Pension and Postretirement Benefits** The Company provides pension and postretirement benefits to certain employees and accounts for these benefits in accordance with ASC 715, *Compensation Retirement Benefits*. For financial reporting purposes, long-term assumptions are developed through consultations with actuaries. Such assumptions include the expected long-term rate of return on plan assets, discount rates, health care trend rates and mortality rates. The discount rate for the current year is based on long-term high quality bond rates.

Table of Contents

**KAPSTONE PAPER AND PACKAGING CORPORATION**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**(\$ in thousands, except share and per share amounts)**

**2. Significant Accounting Policies (Continued)**

**Income Taxes** The Company accounts for income taxes under the liability method in accordance with ASC 740 *Income Taxes*. Accordingly, deferred income taxes are provided for the future tax consequences attributable to differences between the carrying amounts of assets and liabilities for financial reporting and income tax purposes. Deferred tax assets and liabilities are measured using tax rates in effect for the year in which those temporary differences are expected to be recovered or settled. A valuation allowance is established when necessary to reduce deferred tax assets to the amount that is more likely than not to be realized. The Company recognizes the benefit of tax positions when it is more likely than not to be sustained on its technical merits. The Company records interest and penalties on unrecognized tax benefits in the provision for income taxes.

**Amortization of Debt Issuance Costs** The Company capitalizes costs incurred in connection with borrowings or establishment of credit facilities. These costs are amortized over the life of the borrowing or life of the credit facility using the effective interest method. For the years ended December 31, 2014, 2013 and 2012, \$5.7 million, \$4.5 million and \$3.5 million, respectively, of debt issuance costs have been amortized and recognized within interest expense, net.

In 2014, the Company recorded a loss on debt extinguishment of \$5.6 million due to two voluntary prepayments totaling \$325.0 million on the term loans under the Company's senior secured credit facility (the "Credit Facility").

**Stock Based Compensation Expense** The Company accounts for employee stock and stock-based compensation in accordance with ASC 718, *Compensation - Stock Compensation*. Accordingly, compensation expense for the fair value of stock options, as determined on the date of grant, is recorded on an accelerated basis over the awards' vesting periods. The compensation expense for the fair value of restricted stock units, as determined on the date of grant, is recorded on a straight-line basis over the awards' vesting periods. Forfeitures are estimated on the date of grant and revised if actual or expected forfeiture activity differs materially from the original estimate.

**Segment Information** The Company has one operating segment. The Company produces containerboard, corrugated products and specialty paper which are sold to customers who convert our products into end-market finished products or internally to corrugating plants that produce a wide variety of products ranging from basic corrugated shipping containers to specialized packaging.

**Recent Accounting Pronouncements**

In February 2013, the FASB issued ASU 2013-02 "Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income", which amends certain provisions in ASC 220 "Comprehensive Income". These provisions require the disclosure of significant amounts that are reclassified out of other comprehensive income into net income in its entirety during the reporting period. These provisions are effective for fiscal and interim periods beginning after December 15, 2012.

The Company's other comprehensive income / (loss) included reclassification adjustments related to our defined benefit pension plan and other postretirement benefits for the amortization of actuarial gains and losses and prior service costs which are included in cost of sales, excluding depreciation and amortization, in the accompanying Consolidated Statements of Comprehensive Income.

Table of Contents

**KAPSTONE PAPER AND PACKAGING CORPORATION**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**(\$ in thousands, except share and per share amounts)**

**2. Significant Accounting Policies (Continued)**

In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2014-09 "Revenue from Contracts with Customers". The guidance in this update affects any entity that either enters into contracts with customers to transfer goods or services or enters into contracts for the transfer of nonfinancial assets unless those contracts are within the scope of other standards (for example, insurance contracts or lease contracts). The guidance in this update supersedes the revenue recognition requirements in Accounting Standards Codification ("ASC") Topic 605, "Revenue Recognition", and most industry-specific guidance throughout the Industry Topics of the Codification. Additionally, this update supersedes some cost guidance included in Subtopic 605-35, "Revenue Recognition - Construction-Type and Production-Type Contracts". For a public entity, the amendments are effective for annual reporting periods beginning after December 15, 2016, including interim periods within that reporting period. The ASU allows for full or modified retrospective adoption. Early application is not permitted. The Company is currently evaluating the expected impact of adopting this standard.

**3. Longview Acquisition**

On July 18, 2013, the Company acquired 100 percent of the stock of Longview Fibre Paper and Packaging, Inc., ("Longview") for \$1.025 billion plus \$41.5 million of working capital adjustments. Longview is a leading manufacturer of high quality containerboard, kraft papers, and corrugated products. Longview's operations include a paper mill located in Longview, Washington equipped with five paper machines which have the capacity to produce 1.3 million tons of containerboard and kraft paper annually. Longview also owns seven converting facilities located in the Pacific Northwest.

The excess of the purchase price over the aggregate estimated fair value of net assets acquired was allocated to goodwill. The purchase price allocation is final.

Table of Contents**KAPSTONE PAPER AND PACKAGING CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

(\$ in thousands, except share and per share amounts)

**3. Longview Acquisition (Continued)**

The following table summarizes the estimated fair value of the assets acquired and liabilities assumed by major category of assets and liabilities as of December 31, 2013, as well as adjustments (referred to as "measurement period adjustments"):

	Amounts Recognized as of Acquisition Date (as Adjusted)(1)	Measurement Period Adjustments(2)	Amounts Recognized as of Acquisition Date (as Adjusted)
Deposit for redemption of senior notes	\$ 507,520	\$	\$ 507,520
Trade accounts receivable	104,929	42	104,971
Inventories	106,805	(2,026)	104,779
Prepaid expenses and other current assets	2,554		2,554
Plant, property and equipment	800,663	(7,446)	793,217
Pension asset	112,141		112,141
Other receivables and assets	11,863		11,863
Intangible assets	77,600		77,600
Accounts payable	(71,663)		(71,663)
Accrued expenses	(17,630)	80	(17,550)
Accrued compensation costs	(19,385)	61	(19,324)
Debt	(507,520)		(507,520)
Pension and post retirement benefits	(68,105)		(68,105)
Deferred income taxes	(294,086)	3,953	(290,133)
Other noncurrent liabilities	(2,862)		(2,862)
Goodwill	302,935	5,336	308,271
<b>Total acquisition consideration</b>	<b>\$ 1,045,759</b>	<b>\$</b>	<b>\$ 1,045,759</b>

(1) As previously reported in the Notes to Consolidated Financial Statements included in our 2013 Form 10-K.

(2) The measurement period adjustments include the following:

Property, plant, and equipment were adjusted downward by \$7.4 million to reflect the change in fair value estimates for certain acquired equipment.

Inventories were adjusted by \$2.0 million downward to reflect better estimates for replacement parts and supplies.

Deferred income taxes decreased primarily due to the change in property, plant, and equipment and inventories.

The following unaudited pro forma consolidated results of operations assume that the acquisition of Longview occurred as of January 1, 2012. The unaudited pro forma consolidated results includes the accounting effects of the business combination, including the application of the

Company's accounting policies, amortization of intangible assets and depreciation of property, plant and equipment related to

F-15

---

Table of Contents**KAPSTONE PAPER AND PACKAGING CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

(\$ in thousands, except share and per share amounts)

**3. Longview Acquisition (Continued)**

fair value adjustments, interest expense on acquisition related debt, elimination of intercompany sales and income tax effects of the adjustments. The pro forma adjustments are directly attributable to the Longview acquisition, factually supportable and are expected to have a continuing impact on the Company's combined results. Unaudited pro forma data is based on historical information and does not necessarily reflect the actual results that would have occurred, nor is it indicative of future results of operations.

	Years Ended December 31,	
	2013	2012
	(unaudited)	(unaudited)
Net Sales	\$ 2,237,677	\$ 2,047,725
Net Income	\$ 157,367	\$ 103,899

**4. Inventories**

Inventories consist of the following at December 31, 2014 and 2013, respectively:

	December 31,	
	2014	2013
Raw materials	\$ 99,390	\$ 83,136
Work in process	3,634	3,293
Finished goods	63,639	58,336
Replacement parts and supplies	70,026	66,842
Inventories at FIFO costs	236,689	211,607
LIFO inventory reserves	1,640	5,775
Inventories	\$ 238,329	\$ 217,382

At December 31, 2014 and 2013, finished goods inventory included inventory consigned to third parties totaling \$11.9 million and \$8.5 million, respectively.

Table of Contents**KAPSTONE PAPER AND PACKAGING CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

(\$ in thousands, except share and per share amounts)

**5. Plant, Property and Equipment, net**

Plant, property and equipment, net consist of the following at December 31, 2014 and 2013, respectively:

	December 31,	
	2014	2013
Land and land improvements	\$ 74,434	\$ 71,931
Buildings and leasehold improvements	151,542	146,686
Machinery and equipment	1,529,715	1,399,366
Construction-in-process	43,246	70,873
	1,798,937	1,688,856
Less accumulated depreciation and amortization	412,267	299,247
Plant, property, and equipment, net	\$ 1,386,670	\$ 1,389,609

Depreciation expense for the years ended December 31, 2014, 2013, and 2012, was \$122.9 million, \$86.1 million, and \$56.7 million, respectively. The increase in depreciation expense for the year ended December 31, 2014 reflects a full year of the Longview acquisition and higher capital spending.

**6. Goodwill and Other Intangible Assets**

The following table shows changes in goodwill and other intangible assets for the years 2014 and 2013:

	Goodwill	Intangible Assets, Net
Balances at December 31, 2012	\$ 226,289	\$ 57,027
Amortization expense		(10,882)
Longview acquisition	302,935	77,600
Other	(709)	
Balances at December 31, 2013	\$ 528,515	\$ 123,745
Longview acquisition	5,336	
Amortization expense		(13,668)
Balances at December 31, 2014	\$ 533,851	\$ 110,077

Intangible assets other than goodwill include the following:

	December 31, 2014			December 31, 2013		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Definite-lived trademarks	\$ 35,300	\$ (23,276)	\$ 12,024	\$ 35,300	\$ (19,288)	\$ 16,012

Edgar Filing: KAPSTONE PAPER & PACKAGING CORP - Form 10-K

Customer lists and relationships	119,204	(22,440)	96,764	119,204	(12,964)	106,240
Lease, contracts and other	15,943	(14,654)	1,289	15,943	(14,450)	1,493
Total	\$ 170,447	\$ (60,370)	\$ 110,077	\$ 170,447	\$ (46,702)	\$ 123,745

F-17

---



Table of Contents**KAPSTONE PAPER AND PACKAGING CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

(\$ in thousands, except share and per share amounts)

**6. Goodwill and Other Intangible Assets (Continued)**

Estimated amortization expense for the next five years, beginning with 2015, is as follows: \$13.7 million, \$11.9 million, \$10.2 million, \$10.2 million, and \$10.2 million. At December 31, 2014, the weighted average remaining useful life for trademarks is 9 years; customer relationships is 11 years; other contractual agreements is 23 years; and for intangible assets in total is 11 years.

**7. Accrued Expenses**

Accrued expenses consist of the following at December 31, 2014 and 2013, respectively:

	December 31,	
	2014	2013
Energy costs	\$ 10,969	\$ 11,868
Real and property taxes	11,927	5,985
Customer rebates	6,077	5,870
Current postretirement obligation	2,610	4,232
Capital spending	3,445	4,035
Freight	3,465	2,824
Worker's compensation	2,875	2,111
Other accruals	6,972	8,737
Accrued expenses	\$ 48,340	\$ 45,662

**8. Long-term Debt**

Long-term debt consists of the following at December 31, 2014 and 2013, respectively:

	December 31,	
	2014	2013
Term loan A-1 under Amended and Restated Credit Agreement with interest payable monthly at LIBOR plus 1.75% at December 31, 2014	\$ 664,125	\$ 754,938
Term loan A-2 under Amended and Restated Credit Agreement with interest payable monthly at LIBOR plus 2.0% at December 31, 2014	231,113	468,825
Receivable Credit Facility with interest payable monthly at LIBOR plus 0.75% at December 31, 2014	167,000	
Total long-term debt	1,062,238	1,223,763
Less current portion of debt		(4,950)
Less unamortized debt issuance costs	(16,175)	(26,400)
Long-term debt, net of current portion and debt issuance costs	\$ 1,046,063	\$ 1,192,413

Interest paid was \$27.6 million, \$20.5 million, and \$8.3 million, in 2014, 2013 and 2012, respectively. Interest paid was higher in 2014 and 2013 due to higher average term loan balances to fund the Longview acquisition.



Table of Contents**KAPSTONE PAPER AND PACKAGING CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

(\$ in thousands, except share and per share amounts)

**8. Long-term Debt (Continued)**

The principal portion of the total long-term debt at December 31, 2014 becomes due as follows:

<b>Fiscal year ending</b>	
2015	\$
2016	
2017	90,563
2018	740,563
2019	
2020	231,112
<b>Total</b>	<b>\$ 1,062,238</b>

**Receivables Credit Facility**

In September 2014, certain wholly-owned subsidiaries of the Company ("Originators") entered into a one-year agreement to sell certain trade receivables (the "Receivables") on a non-recourse basis (subject to purchase price credits for breaches of certain representations and warranties with respect to the Receivables), to KapStone Receivable, LLC ("KAR"), a wholly-owned subsidiary of the Company that is a bankruptcy remote variable interest entity ("VIE"). KAR is a variable interest entity as it receives subordinated financing from the Originators from time to time to finance its activities. The Company continues to service the receivables after they have been sold to KAR and makes the primary decisions regarding the collateral in KAR and is therefore the primary beneficiary and consolidates the account balances of KAR. Sales of Receivables to KAR occur daily and are settled on a monthly basis. KAR finances its purchases of the Receivables in part with proceeds of draws under a one-year facility ("Receivables Credit Facility"), subject to a maximum of \$175 million. The actual amount available to draw upon varies based on eligible receivables (as defined in the documents establishing the Receivables Credit Facility). KAR pays a fee for the drawn and undrawn portions of the Receivables Credit Facility, respectively.

KAR's sole business consists of the purchase of the Receivables from the Originators, through a combination of draws under the Receivables Credit Facility, draws on subordinated notes payable to the Originators and capital contributions from one of the Originators, and the subsequent sale of undivided ownership interests in, or granting of a security interest in, such Receivables to the bank agent under the Receivables Credit Facility. KAR is a separate legal entity with its own separate creditors who will be entitled, upon liquidation, to be satisfied out of KAR's assets prior to any assets or value in KAR becoming available to the Originators or the Company, and the assets of KAR are not available to pay creditors of the Company or any of its affiliates (other than KAR).

At December 31, 2014, \$225.7 million of the Company's trade accounts receivables were sold to KAR and \$167.0 million of borrowings were outstanding and included in Long-term debt on the Consolidated Balance Sheets.

The Company included the Receivables Credit Facility in Long-term debt on the Consolidated Balance Sheets based on management's intent to continue to refinance this agreement until the maturity of the Term loan A-1 which is July 18, 2018. The Company also has the ability to refinance this short-term obligation on a long-term basis using its Revolving Credit Facility. There are no

Table of Contents

**KAPSTONE PAPER AND PACKAGING CORPORATION**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**(\$ in thousands, except share and per share amounts)**

**8. Long-term Debt (Continued)**

additional requirements as to when borrowings under the Revolver would need to be repaid other than the maturity date of July 18, 2018.

The Company incurred approximately \$0.4 million of fees associated with the Receivable Credit Facility, which have been deferred and will be amortized as interest expense using the effective interest method.

The proceeds from the Receivables Credit Facility were used to prepay \$175.0 million of the term loans and as a result, \$3.0 million of unamortized debt issuance costs were written-off as a loss on debt extinguishment.

**Amendments to the Amended and Restated Credit Agreement**

In April 2014, the Company entered into a First Amendment (the "First Amendment") to the Amended and Restated Credit Agreement dated as of July 18, 2013 (as amended from time to time, the Amended and Restated Credit Agreement). The First Amendment reduced the borrowing rates under our Credit Facility for both term loans under the Credit Facility and for any future borrowings under the \$400 million revolving credit facility (the "Revolver") portion of the Credit Facility. The interest rates are based on LIBOR rates plus a margin determined from a pricing grid based on the Company's debt to EBITDA ratio as defined in our Amended and Restated Credit Agreement. Accordingly, the weighted average interest rate on borrowings under the Credit Facility as of December 31, 2014 is 1.98 percent, compared to 2.25 percent as of March 31, 2014. The First Amendment also reduced the unused commitment fees related to the Revolver by 5 to 10 basis points.

The Company incurred approximately \$0.7 million of fees associated with the First Amendment, which have been deferred and are being amortized as interest expense using the effective interest method.

In August 2014, the Company entered into a Second Amendment to the Amended and Restated Credit Agreement, which included certain technical amendments to the Amended and Restated Credit Agreement in connection with the Receivables program and the related Receivables Credit Facility.

In December 2014, the Company entered into a Third Amendment to the Amended and Restated Credit Agreement. The modification of the Amended and Restated Credit Agreement will enable the Company, subject to certain conditions and limitations to pay dividends on, or make repurchases of, the Company's common stock.

In December 2014, the Company made \$150.0 million of voluntary prepayment on its term loans under the credit facility and as a result, \$2.6 million of unamortized debt issuance costs were written-off as a loss on debt extinguishment.

**Revolver**

As of December 31, 2014, the Company had no amounts outstanding under the Revolver under the Amended and Restated Credit Agreement with current availability of \$395.7 million.

Table of Contents

**KAPSTONE PAPER AND PACKAGING CORPORATION**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**(\$ in thousands, except share and per share amounts)**

**8. Long-term Debt (Continued)**

**Debt Covenants**

The Amended and Restated Credit Agreement contains, among other provisions, covenants with which we must comply. The covenants limit our ability to, among other things, incur indebtedness, create additional liens on our assets, make investments, engage in mergers and acquisitions, pay dividends and sell any assets outside the normal course of business.

As of December 31, 2014, the Company was in compliance with all applicable covenants in the Amended and Restated Credit Agreement.

**Fair Value of Debt**

As of December 31, 2014, the fair value of the Company's debt approximates the carrying value of \$1.1 billion as the variable interest rates re-price frequently at current market rates. The debt was valued using Level 2 inputs in the fair value hierarchy which are significant observable inputs including quoted prices for debt of similar terms and maturities.

**Other Current Borrowing**

In 2014 and 2013, the Company entered into financing agreements of \$6.3 million and \$5.1 million, respectively, at an annual interest rate of 1.69 and 1.61 percent, respectively, for its annual property insurance premiums. These agreements required the Company to pay consecutive monthly payments through the term of each financing agreement ending on December 1st of each year.

**9. Pension and Postretirement Benefits**

The Company and its subsidiaries had three defined benefit retirement plans ("Plan") for certain eligible employees. These plans were merged into the KapStone defined benefit plan effective December 31, 2014.

The legacy KapStone defined benefit plan provides benefits based on years of credited service and stated dollar level multipliers for each year of service. We also sponsor postretirement plans which provide certain medical and life insurance benefits ("other benefits") to qualifying union employees.

In conjunction with the Longview acquisition, the Company acquired two defined benefit plans, one for non-union employees and the other for hourly union employees. The Longview plan covering certain salaried and non-union hourly employees is a cash balance plan providing benefits at ten percent of eligible earnings. This plan was frozen on December 31, 2014. Effective December 31, 2010, benefits under the plan covering a majority of union employees were frozen. Cash balance contributions were made for certain eligible employees in 2014, 2013 and 2012. The one union with an active benefit is eligible for a stated dollar multiplier per years of eligible service.

The liabilities for the benefit obligation for the eligible union groups are based on the collective bargaining agreements currently in effect. Future negotiations on collective bargaining agreements could have an effect on these liabilities.

Table of Contents**KAPSTONE PAPER AND PACKAGING CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

(\$ in thousands, except share and per share amounts)

**9. Pension and Postretirement Benefits (Continued)**

The changes in benefit obligations and Plan assets at December 31, 2014 and 2013 were:

	Pension Benefits		Other Benefits	
	2014	2013	2014	2013
<b>Change in Benefit Obligation</b>				
Benefit obligation at beginning of year	\$ 577,706	\$ 29,140	\$ 20,847	\$ 1,361
Longview acquisition		559,538		21,634
Service cost	9,886	8,274	34	47
Interest cost	28,847	13,555	627	354
Actuarial loss (gain)	92,156	(16,527)	(4,366)	(9)
Participant contributions			742	505
Benefits paid	(39,419)	(17,019)	(4,184)	(3,045)
Plan amendment	49	745		
Benefit obligation at end of year	\$ 669,225	\$ 577,706	\$ 13,700	\$ 20,847
<b>Change in Plan Assets</b>				
Fair value of plan assets at beginning of year	\$ 645,490	\$ 17,414	\$	\$
Longview acquisition		620,546		
Actual return on plan assets	37,921	21,739		
Employer contributions	3,523	2,810	3,442	2,540
Participant contributions			742	505
Benefits paid	(39,419)	(17,019)	(4,184)	(3,045)
Fair value of plan assets at end of year	\$ 647,515	\$ 645,490	\$	\$

Table of Contents

## KAPSTONE PAPER AND PACKAGING CORPORATION

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(\$ in thousands, except share and per share amounts)

## 9. Pension and Postretirement Benefits (Continued)

The funded status and amounts recognized in our Consolidated Balance Sheets at December 31, 2014 and 2013 were:

	Pension Benefits		Other Benefits	
	2014	2013	2014	2013
<b>Funded Status at End of Year</b>	\$ (21,710)	\$ 67,784	\$ (13,700)	\$ (20,847)

**Amounts Recognized in Consolidated Balance Sheets:**

Other assets	\$	\$ 120,780	\$	\$
Accrued expenses			(2,610)	(4,232)
Pension and postretirement benefits	(21,710)	(52,996)	(11,090)	(16,615)
<b>Net amount recognized</b>	\$ (21,710)	\$ 67,784	\$ (13,700)	\$ (20,847)

**Amounts Recognized in Accumulated Other Comprehensive Income / (Loss) (Pre-tax)**

Total net actuarial (gain) loss	\$ 86,691	\$ (11,687)	\$ (4,208)	\$ 147
Prior service cost	392	745	(1,086)	(1,286)
<b>Total</b>	\$ 87,083	\$ (10,942)	\$ (5,294)	\$ (1,139)

**Weighted-Average Discount Rate Assumption used to Determine**

<b>Projected Benefit Obligations at December 31, 2014 and 2013</b>	<b>4.24%</b>	<b>5.11%</b>	<b>3.78%</b>	<b>4.83%</b>
--	--------------	--------------	--------------	--------------

The accumulated benefit obligation for the defined benefit pension plan was \$699.2 million and \$577.7 million at December 31, 2014 and 2013, respectively.

The Company's pension plan funded status decreased by \$89.0 million in 2014 reflecting \$66.3 million due to a lower discount rate and \$27.8 million due to the change mortality assumptions. In 2014, we considered the new mortality tables from the Society of Actuaries and evaluated our mortality experience to establish mortality assumptions. Based on our experience and in consultation with our actuaries, we utilized a base RP-2014 with MP-2014 projection scale and appropriate collar adjustments. In 2013, we utilized the RP-2000 mortality tables.

Components of pension and other postretirement benefit (income)/costs were:

	Pension Benefits			Other Benefits		
	2014	2013	2012	2014	2013	2012
Service cost	\$ 9,886	\$ 8,274	\$ 4,094	\$ 34	\$ 47	\$ 36
Interest cost	28,847	13,555	1,007	627	354	63
Expected return on plan assets	(44,143)	(20,851)	(934)			
Amortization of prior service cost (benefit)	403	130	368	(200)	(200)	(200)
Amortization of net loss (gain)		289	215	(11)	20	45

Edgar Filing: KAPSTONE PAPER & PACKAGING CORP - Form 10-K

Benefit (income)/cost	Company plans	(5,007)	1,397	4,750	450	221	(56)
Pension benefit cost	multi-employer plan	333	325	86			
Total benefit (income)/cost		\$ (4,674)	\$ 1,722	\$ 4,836	\$ 450	\$ 221	\$ (56)

F-23

---



Table of Contents**KAPSTONE PAPER AND PACKAGING CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

(\$ in thousands, except share and per share amounts)

**9. Pension and Postretirement Benefits (Continued)**

Weighted-Average actuarial assumptions used to determine benefit costs were:

	Pension Benefits			Other Benefits		
	2014	2013	2012	2014	2013	2012
Discount rate	5.11%	4.77%	4.64%	4.83%	3.26%	4.64%
Long-term rate of return on plan assets	6.98%	6.25%	6.50%			

The Company assumed health care cost trend rates for its postretirement benefits plans were as follows:

Plans	2015
Health care cost trend rate assumed for next year	6.50%
Rate to which the cost trend rate is assumed to decline (the ultimate rate)	4.50%
Year the rate reaches the ultimate trend rate	2019

The effect of a one percentage point increase or decrease in the assumed health care cost trend rates at December 31, 2014 is summarized below:

Change in Health Care	Minus 1%	Plus 1%
Service and interest cost	\$ (20)	\$ 21
Accumulated benefit obligation	\$ 371	\$ 392

Other changes in Plan assets and benefit obligations recognized in accumulated other comprehensive (income) loss were:

	Pension Benefits		Other Benefits	
	2014	2013	2014	2013
Net actuarial (gain) loss	\$ 98,378	\$ (17,415)	\$ (4,366)	\$ (9)
Plan amendment	49	745		
Amortization of prior service (cost) benefit	(402)	(130)	200	200
Amortization of net gain (loss)		(289)	11	(20)
Net amount recognized before tax	\$ 98,025	\$ (17,089)	\$ (4,155)	\$ 171

The amounts in accumulated other comprehensive income (loss) expected to be recognized as components of net expense during 2015 are as follows:

	Pension Benefits	Other Benefits
Prior service cost (benefit)	\$ 275	\$ (200)
Net actuarial loss / (gain)	\$ 2,135	\$ (909)

For pension plans, accumulated actuarial gains and losses in excess of 10 percent of the accumulated benefit obligation and prior service cost are amortized over the average future service period of approximately 9 years.

Table of Contents**KAPSTONE PAPER AND PACKAGING CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

(\$ in thousands, except share and per share amounts)

**9. Pension and Postretirement Benefits (Continued)**

As of December 31, 2014 and 2013, \$(52.0) million and \$7.5 million, respectively, were included net of tax in accumulated other comprehensive income (loss).

**Plan Assets**

The fair value of Plan assets, summarized by level within the fair value hierarchy as of December 31, 2014 was as follows:

	Level 1	Level 2	Level 3	Total
Cash and cash equivalents	\$ 37,302	\$	\$	\$ 37,302
Equity securities:				
Common stock	10,387			10,387
Balance mutual funds	30,795			30,795
International equity mutual funds	46,701			46,701
U.S. large cap collective funds		75,709		75,709
Fixed income:				
Corporate bonds and notes:				
Short-term		14,349		14,349
Mid-term		35,884		35,884
Long-term		159,453		159,453
U.S. Government securities :				
Short-term		8,657		8,657
Mid-term		8,555		8,555
Long-term		65,234		65,234
Hedge funds:				
Fixed income funds		16,726	32,475	49,201
Equity funds		24,973	56,480	81,453
Limited partnership investments			23,835	23,835
Total assets	\$ 125,185	\$ 409,540	\$ 112,790	\$ 647,515

Table of Contents**KAPSTONE PAPER AND PACKAGING CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

(\$ in thousands, except share and per share amounts)

**9. Pension and Postretirement Benefits (Continued)**

The table below presents a summary of changes in the fair value of the Plans' level three assets as of December 31, 2014:

<b>Year ended December 31, 2014</b>	<b>Real Estate</b>	<b>Limited Partnership Investments</b>	<b>Equity Hedge Funds</b>	<b>Fixed Income Hedge Funds</b>
Balance, beginning of year	\$ 24,412	\$ 25,548	\$	\$
Transfers into Level 3				
Transfers out of Level 3				
Total gains or (losses):				
Included in changes in net assets	2,163	3,687	(1,420)	(1,325)
Included in other comprehensive income				
Purchases, issuances, sales, and settlements:				
Purchases		1,205	57,900	33,800
Issuances				
Sales	(26,575)	(6,605)		
Settlements				
Balance, end of year	\$	\$ 23,835	\$ 56,480	\$ 32,475

The amount of total gains or losses for the year included in changes in net assets attributed to the change in unrealized gains or losses relating to assets still held at the reporting date.	\$ 1,402	\$ 2,452	\$ (1,420)	\$ (1,325)
--	----------	----------	------------	------------

Table of Contents**KAPSTONE PAPER AND PACKAGING CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

(\$ in thousands, except share and per share amounts)

**9. Pension and Postretirement Benefits (Continued)**

The fair value of Plan assets, summarized by level within the fair value hierarchy as of December 31, 2013 was as follows:

	Level 1	Level 2	Level 3	Total
Cash and cash equivalents	\$ 58,194	\$	\$	\$ 58,194
Equity securities:				
Common stock	16			16
U.S. large cap	25,565			25,565
U.S. mid cap	4,666			4,666
Emerging market large cap	5,121			5,121
Global real estate	50,456			50,456
Foreign large cap	72,067			72,067
Foreign mid growth	930			930
Fixed income:				
Corporate bonds and notes:				
Short-term		144,438		144,438
Mid-term	5,960	136,412		142,372
Long-term	1,049	13,586		14,635
Emerging market bonds	1,465			1,465
U.S. Government securities (short-term)	33,187	29,916		63,103
Mortgage backed securities		10,404		10,404
Real estate		1,092	24,412	25,504
Limited partnership investments			25,548	25,548
Other	1,006			1,006
<b>Total assets</b>	<b>\$ 259,682</b>	<b>\$ 335,848</b>	<b>\$ 49,960</b>	<b>\$ 645,490</b>

Level 1 assets are valued based on quoted prices in active markets for identical securities.

Level 2 assets are valued based on other significant observable inputs including quoted prices for similar securities, yield curves, indices, etc. Level 2 assets listed above consist primarily of commingled equity investments where values are based on the net asset value of the underlying investments held, individual fixed income securities where values are based on quoted prices of similar securities and observable market data, and commingled fixed income investments where values are based on the net asset value of the underlying investments held.

Level 3 assets are valued based on unobservable inputs. Quoted market prices are not available for certain investments, including real estate and limited partnership investments. These investments are recorded at their estimated fair market value; therefore, the reported value may differ from the value that would have been used had a quoted market price existed. Investments of this nature are valued by the Company based on the nature of each investment and the information available to management at the valuation date.

Limited Partnership investments generally have limited liquidity and are made through long-term partnerships or joint ventures that invest in pools of capital invested in primarily non-publicly traded

Table of Contents**KAPSTONE PAPER AND PACKAGING CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

(\$ in thousands, except share and per share amounts)

**9. Pension and Postretirement Benefits (Continued)**

entities. Underlying investments include venture capital, buyout, and special situations investing. Private equity management firms typically acquire and then reorganize private companies to create increased long-term value. Valuation is based on statements received from the investment managers, transaction data, analysis of and judgments about underlying investments and other third-party information deemed reliable for the purposes of developing an estimate of fair market value.

Hedge funds are privately owned institutional investment funds that generally have moderate liquidity. Hedge funds seek specified levels of return, regardless of market conditions, and generally have a low correlation to public equity and debt markets. Hedge funds often invest substantially in financial market instruments (stocks, bonds, commodities, currencies, derivatives, etc.) using a broad range of trading activities to manage portfolio risks. Plan holdings in hedge funds are valued using the net asset value ("NAV") provided by the administrator of the fund and reviewed by the Company. The NAV per share is based on the value of the underlying assets owned by the fund, minus liabilities and divided by the number of shares or units outstanding. These assets are reported at NAV as a practical expediency and are classified as Level II or Level III based on the liquidity of the investments. For the year ended December 31, 2014, the Plan held \$69.3 million of hedge funds with restrictions on redemption for the first year after funds are invested, and \$19.7 million of hedge funds restricting investment redemption to a 25 percent gate in any given quarter. Limited liquidity hedge funds are classified as Level 3.

The Company believes that the reported amounts for these investments are a reasonable estimate of their fair value at December 31, 2014. However, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value at the reporting date.

To develop the expected long-term rate of return on plan assets for the pension plan, the Company considers the target asset allocation, the historical investment performance, and the expectations for future returns of each asset class.

The Company's pension plan weighted-average asset allocations and target asset allocations at December 31, 2014 and 2013, by asset category were as follows:

	2014	2013	Target Allocation
Fixed income	53%	58%	53%
Equity securities	38%	25%	41%
Real estate	%	4%	%
Cash	6%	9%	%
Other	3%	4%	6%
Total	100%	100%	100%

The Company's investment goals are to provide a total return that, over the long term, increases the ratio of plan assets to liabilities subject to an acceptable level of risk. This is accomplished through diversification of assets in accordance with the Investment Policy guidelines. Investment risk is mitigated by periodic rebalancing between asset classes as necessitated by changes in market conditions within the Investment Policy guidelines.

Table of Contents**KAPSTONE PAPER AND PACKAGING CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

(\$ in thousands, except share and per share amounts)

**9. Pension and Postretirement Benefits (Continued)**

The Company currently anticipates making contributions of approximately \$1.1 million in 2015. This estimate is based on current tax laws, plan asset performance, and liability assumptions, which are subject to change. The Company anticipates making contributions to the postretirement plans in 2015 as claims are submitted.

The following table presents estimated future benefit payments for the Company's plans:

	<b>Pension Benefits</b>	<b>Other Benefits</b>
2015	\$ 36,908	\$ 2,660
2016	37,400	2,217
2017	38,262	1,880
2018	39,042	1,519
2019	40,137	1,305
Succeeding 5 years	204,555	3,579

**Postretirement Benefits Other Than Pensions**

In conjunction with the Longview acquisition, the Company assumed a liability of \$21.6 million for the Longview Retiree Medical Benefits Plan. This plan provides postretirement health care insurance benefits through an indemnity plan and a health maintenance organization ("HMO") plan for certain salary and non-salary legacy Longview employees and their dependents. Individual benefits generally continue until age 65. Effective for the majority of union employees active on June 1, 2010, the Company amended the plan such that postretirement health care insurance benefits terminated on December 31, 2013. The Company does not pre-fund these benefits, and, accordingly, there are no postretirement plan assets. The postretirement plan also includes a retiree contribution requirement for certain salaried and certain hourly employees. The retiree contribution amount is adjusted annually.

**Multiemployer Pension Plan**

In conjunction with each of the Longview and USC acquisitions, the Company assumed participation in the GCIU-Employer Retirement Fund (formerly IP&GCU Employer Retirement Fund) (the "GCIU Fund") for hourly employees at four plant locations. The GCIU Fund is a multiemployer defined benefit retirement plan established for employers and unions in the newspaper, commercial printing, printing specialties and paper products industries that have entered into collective bargaining agreements wherein provisions are made for contributions to be made by the employers to provide retirement benefits to eligible employees or their beneficiaries.

The risks of participating in the multiemployer plan are different from single-employer plans. Unlike single employer plans, assets contributed to a multiemployer plan by one employer may be used to provide benefits to employees of other plan participants. All contributions to this plan are made solely by participating employers. As such, if a participating employer stops contributing to the plan, the Company may be liable for the related unfunded obligations. If the Company chooses to stop participating in the multiemployer plan, the Company may be required to pay the plan an amount based on the unfunded status of the plan. For more information related to the plan, the U.S. Department of Labor makes IRS filings and actuarial reports available to the public.

Table of Contents**KAPSTONE PAPER AND PACKAGING CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

(\$ in thousands, except share and per share amounts)

**9. Pension and Postretirement Benefits (Continued)**

The contribution schedule for the multiemployer plan is determined by the collective bargaining agreements between participating employers and participating unions. The Company does not determine the actuarial present value of accumulated plan benefits, as net assets available for benefits allocable to the individual participating employers are determined by reference to the multiemployer plan's funding status as a whole. The Company makes contributions to the multiemployer plan in accordance with its contribution schedule, including employer surcharges and additional contributions resulting from the multiemployer plan's adoption of a rehabilitation plan effective November 1, 2009.

The multiemployer plan has a fiscal year end of December 31, which may impact financial information available as of December 31, 2014. The contributions made by the Company were less than 4.0 percent of the total employers' contributions to the multiemployer plan for the plan year ended December 31, 2013, the most recent date for which information was available.

Pension Fund	Federal EIN	Pension Protection Act Zone Status			FIP / RP Status Pending / Implemented	Contributions by the Company for the period Ended December 31,			Surcharge Imposed	Expiration Date of Collective-Bargaining Agreement
		2014	2013	2012		2014	2013	2012		
GCIU-Employer Retirement Fund	91-6024903	Critical	Critical	Critical	Implemented	\$ 333	\$ 339	\$ 86	Yes	Varies 6/16/2014 thru 10/21/2015

According to the audited financial statements of the multiemployer plan, the net assets available for benefits were \$1,150 million and \$1,063 million as of December 31, 2013 and 2012, respectively. An independent actuarial valuation calculated the actuarial present value of accumulated plan benefits to be \$1,655 million and \$1,654 million as of January 1, 2013 and 2012, respectively. As of December 31, 2014, the Company was unable to obtain the estimated withdrawal liability from the multiemployer plan's actuary. At December 31, 2013, the Company's estimated withdrawal liability was \$50.1 million. The Company has no plans to withdraw from the plan at this time. In accordance with ASC 715, *Compensation Retirement Benefits*, this potential liability is not recognized in the Company's Consolidated Balance Sheets.

**Defined Contribution Plan**

Certain employees are covered under a 401(k) defined contribution plan. The expense related to this plan was \$15.1 million, \$12.3 million, and \$11.2 million for the years ended December 31, 2014, 2013, and 2012, respectively.

In conjunction with the Longview acquisition, the Company acquired two additional savings plans. These savings plans allow certain employees salary deferrals in accordance with section 401(k) of the Internal Revenue Code of 1986, as amended. The Company makes a contribution equal to between 2 percent and 3 percent respectively, of the certain eligible union employee's earnings. Effective in 2015 former Longview salaried personnel will receive a 401(k) contribution rather than a cash balance plan contribution.

Table of Contents**KAPSTONE PAPER AND PACKAGING CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

(\$ in thousands, except share and per share amounts)

**10. Income taxes**

The Company's U.S. federal statutory tax rate was 35.0 percent for each of 2014, 2013, and 2012. The Company's effective income tax rate for the years ended December 31, 2014, 2013, and 2012 were 34.0 percent, 34.7 percent, and 35.9 percent, respectively. Substantially all income was earned in the United States.

The Company's provision for income taxes for the years ended December 31, 2014, 2013, and 2012 consists of the following:

	Years Ended December 31,		
	2014	2013	2012
<b>Current:</b>			
Federal	\$ 78,105	\$ 2,384	\$ 10,213
State	8,126	5,403	1,637
<b>Total current</b>	<b>86,231</b>	<b>7,787</b>	<b>11,850</b>
<b>Deferred:</b>			
Federal	\$ 826	\$ 53,404	\$ 22,794
State	1,629	6,461	334
<b>Total deferred</b>	<b>2,455</b>	<b>59,865</b>	<b>23,128</b>
<b>Total provision for income taxes</b>	<b>\$ 88,686</b>	<b>\$ 67,652</b>	<b>\$ 34,978</b>

Income taxes paid, net of refunds, were \$77.5 million, \$4.0 million, and \$7.0 million in 2014, 2013 and 2012, respectively. The increase in 2014 income taxes paid is due to higher pre-tax income following the 2013 Longview acquisition, significant tax credit carry-forwards and net operating losses fully utilized through 2013, and bonus depreciation claimed in 2013.

The Company's effective income tax rate differs from the statutory federal income tax rate as follows:

	Years Ended December 31,		
	2014	2013	2012
Statutory tax rate	35.0%	35.0%	35.0%
State income taxes, net of federal income tax benefit	2.1%	2.9%	2.1%
Deferred tax adjustments due to tax rate changes	0.5%	1.2%	(0.7)%
Domestic manufacturing deduction	(3.0)%	(2.0)%	(0.9)%
Changes in uncertain tax positions	(0.1)%	(2.6)%	
Other	(0.5)%	0.2%	0.4%
<b>Effective income tax rate</b>	<b>34.0%</b>	<b>34.7%</b>	<b>35.9%</b>

For the years ended December 31, 2014, 2013, and 2012, respectively, the Company's effective income tax rate included a 0.5 percent deferred tax expense from changes in apportioned state rates that adjusted deferred tax liabilities, a 1.2 percent deferred tax expense as a result of



state tax rate

F-31

---

Table of Contents**KAPSTONE PAPER AND PACKAGING CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

(\$ in thousands, except share and per share amounts)

**10. Income taxes (Continued)**

changes due to the Longview acquisition and a (0.7) percent deferred tax benefit as a result of the USC acquisition.

The tax effects of the temporary differences that give rise to significant portions of the deferred tax assets and liabilities at December 31, 2014 and 2013, for the Company are as follows:

	Years Ended December 31,	
	2014	2013
Deferred tax assets resulting from:		
Accrued compensation costs	\$ 7,368	\$ 5,697
Acquisition transaction costs	872	995
Pension and postretirement benefits	14,450	
Stock based compensation	6,073	4,571
Tax credit carry-forwards	1,692	2,982
State net operating loss carry-forwards	263	519
Other	2,983	2,399
<b>Total deferred tax assets</b>	<b>\$ 33,701</b>	<b>\$ 17,163</b>
Valuation allowance		
<b>Net deferred tax assets</b>	<b>\$ 33,701</b>	<b>\$ 17,163</b>
Deferred tax liabilities resulting from:		
Inventories	(10,906)	(10,767)
Prepaid expenses	(1,928)	(1,927)
Pension and postretirement benefits		(14,904)
Depreciable assets	(398,072)	(397,571)
Intangible assets	(27,466)	(33,937)
Goodwill	(9,612)	(8,174)
<b>Total deferred tax liabilities</b>	<b>\$ (447,984)</b>	<b>\$ (467,280)</b>
<b>Net deferred tax liabilities</b>	<b>\$ (414,283)</b>	<b>\$ (450,117)</b>

At December 31, 2014 and 2013, the Company had the following net deferred tax liabilities on the Consolidated Balance Sheets:

	Years Ended December 31,	
	2014	2013
Current deferred tax liability, net	\$ (1,990)	\$ (5,445)
Non-current deferred tax liabilities	(412,293)	(444,672)

Edgar Filing: KAPSTONE PAPER & PACKAGING CORP - Form 10-K

Net deferred tax liabilities	\$	(414,283)	\$	(450,117)
------------------------------	----	-----------	----	-----------

The Company accounts for income taxes in accordance with ASC 740, Income Taxes, which provides that a tax benefit from an uncertain tax position may be recognized when it is more likely

F-32

---

Table of Contents**KAPSTONE PAPER AND PACKAGING CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

(\$ in thousands, except share and per share amounts)

**10. Income taxes (Continued)**

than not that the position will be sustained upon examination, including resolution of any related appeals or litigation processes, based on the technical merits. Additionally, for uncertain tax positions, a threshold condition must be met for any part of the benefit of such a position to be recognized in the financial statements.

The Company has \$0.3 million of state tax net operating loss carry-forwards which are available to reduce future taxable income in various state jurisdictions and expire between 2015 and 2030.

The Company has \$1.7 million of state tax credit carry-forwards which expire between 2016 and 2034.

The following is a reconciliation of the total amount of unrecognized tax benefits:

	Years Ended December 31,	
	2014	2013
Unrecognized tax benefits at beginning of year	\$ 730	\$ 4,977
Gross increase tax positions prior period	251	
Gross decrease tax positions prior period	(279)	(4,977)
Gross increase tax positions current period	222	
Longview acquisition		730
Lapse of statute of limitations	(405)	
Settlements		
Unrecognized tax benefits at end of year	\$ 519	\$ 730

In June 2014, the Internal Revenue Service ("IRS") concluded their examination of Longview's tax returns for 2011, 2012, and the period ending with our acquisition in July 2013. As a result, the Company reversed a \$0.3 million reserve for an uncertain tax position in the second quarter. In October 2014, a state statute of limitations lapsed and as a result the Company reversed a \$0.4 million reserve for an uncertain tax position in the fourth quarter.

Total unrecognized tax benefits as of December 31, 2014 and December 31, 2013 were \$0.5 million and \$0.7 million, respectively. As of December 31, 2014, \$0.5 million would impact the effective income tax rate if recognized. Total accrued interest and penalties as of December 31, 2014 and December 31, 2013, were approximately \$0.1 million. As of December 31, 2014 and December 31, 2013, unrecognized tax benefits and related accrued interest were included in other liabilities in the accompanying Consolidated Balance Sheets. The Company does not expect a material change in its unrecognized tax benefits within the next twelve months.

In the normal course of business, the Company is subject to examination by taxing authorities. The Company's open federal tax years are 2011 and 2013, as the IRS completed their examination of the 2012 year during the third quarter of 2014. All IRS examinations of pre-acquisition tax periods for Longview and US Corrugated have been completed (Longview during the second quarter; US Corrugated at the end of the year). The Company has open tax years for state income tax filings generally starting in 2011.

Table of Contents

**KAPSTONE PAPER AND PACKAGING CORPORATION**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**(\$ in thousands, except share and per share amounts)**

**11. Stockholder's equity**

**Employee Stock Purchase Plan**

In December 2009, the Company established the KapStone Paper and Packaging Corporation Employee Stock Purchase Plan ("ESPP"), effective January 1, 2010. The ESPP allows for employees to purchase shares of Company stock at a five percent discount from market price. A total of 1,000,000 shares were reserved for future purchases under the ESPP (amount reflects the stock split announce in December 2013). A total of 20,488 shares and 25,240 shares were issued under the ESPP for the years ended December 31, 2014 and 2013, respectively.

**Common Stock Reserved for Issuance**

At December 31, 2014, approximately 5.0 million shares of common stock were reserved for issuance including 4.1 million shares for stock awards and 0.9 million shares for the ESPP.

**Cash Dividends**

On December 16, 2014, the Company's board of directors approved and declared a regular quarterly dividend of \$0.10 per share. The dividend for the fourth quarter was paid on January 12, 2015. The Company paid \$0.2 million of cash dividends during 2014 related to the 2012 special cash dividend for restricted stock units that vested during the year.

On November 28, 2012, the Company's board of directors approved a \$1.00 per share special cash dividend payable to all shareholders of record as of December 10, 2012 (which reflects the stock split declared in December 2013). The special cash dividend of \$94.9 million was paid on December 20, 2012.

**Stock Split**

On December 11, 2013, the Company's board of directors declared a two-for-one stock split in the form of a stock dividend on the Company's common stock (the "stock split"). To implement the stock split, one share of common stock for each then-outstanding share of common stock was distributed on January 7, 2014 to all shareholders of record as of the close of business on December 23, 2013. The consolidated financial statements and related footnotes have been adjusted for all periods presented to reflect the stock split.

**12. Stock-Based Compensation**

**Share-Based Plan**

On May 15, 2014, stockholders of the Company approved the 2014 Incentive Plan ("2014 Plan"). The major differences between the 2014 Plan and the Amended and Restated 2006 Incentive plan are that under the 2014 Plan:

An increase in the maximum number of shares to 8,500,000 shares of our common stock which will initially be available for all awards, subject to adjustment in the event of certain corporate transactions described in the 2014 Plan.

Table of Contents**KAPSTONE PAPER AND PACKAGING CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

(\$ in thousands, except share and per share amounts)

**12. Stock-Based Compensation (Continued)**

To the extent the Company grants a stock option or SAR under the 2014 Plan, the number of shares of common stock that remain available for future grants will be reduced by an amount equal to the number of shares subject to such stock option or SAR.

To the extent the Company grants restricted stock or a restricted stock unit (collectively, "Stock Awards") under the 2014 Plan, the number of shares of common stock that remain available for future grants will be reduced by an amount equal to two times the number of shares subject to such Stock Award.

Under the 2014 Plan, awards may be granted to employees, officers and directors of, and consultants and advisors to, the Company.

As of December 31, 2014, approximately 4.1 million shares were reserved for granting additional stock options, restricted stock awards or stock appreciation rights. If any award is forfeited or expires without being exercised, or if restricted stock is repurchased by the Company, the common shares subject to the award shall be available for additional grants under the Incentive Plan. The number of shares available under the Incentive Plan is subject to adjustment in the event of any stock split, stock dividend, recapitalization, spin-off or other similar action. Awards may be granted to employees, officers and directors of, and consultants or advisors to, the Company. Options intended to qualify, under the standards set forth in certain federal tax rules, as incentive stock options ("ISOs") may be granted only to employees while actually employed by the Company. Non-employee directors, consultants and advisors are not entitled to receive ISOs. Option awards granted under the Incentive Plan are exercisable for a period fixed by the administrator, but no longer than 10 years from the date of grant, at an exercise price which is not less than the fair market value of the shares on the date of the grant.

The compensation committee of the board of directors approves all stock awards. The Company accounts for stock awards in accordance with ASC 718, *Compensation - Stock Compensation*, which requires that the cost resulting from all share-based payment transactions be recognized as compensation cost over the vesting period based on the fair value of the instrument on the date of grant.

Total non-cash stock-based compensation expense related to stock options and restricted stock for the years ended December 31, 2014, 2013 and 2012 is as follows:

	Years Ended December 31,		
	2014	2013	2012
Stock option compensation expense	\$ 3,595	\$ 2,830	\$ 2,910
Restricted stock unit compensation expense	3,361	2,373	2,332
<b>Total stock-based compensation expense</b>	<b>\$ 6,956</b>	<b>\$ 5,203</b>	<b>\$ 5,242</b>

Table of Contents**KAPSTONE PAPER AND PACKAGING CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

(\$ in thousands, except share and per share amounts)

**12. Stock-Based Compensation (Continued)**

Total unrecognized stock-based compensation cost related to the stock options and restricted stock as of December 31, 2014 and 2013 is as follows:

	December 31,	
	2014	2013
Unrecognized stock option compensation expense	\$ 3,243	\$ 2,250
Unrecognized restricted stock unit compensation expense	3,923	2,535
<b>Total unrecognized stock-based compensation expense</b>	<b>\$ 7,166</b>	<b>\$ 4,785</b>

As of December 31, 2014, total unrecognized compensation cost related to non-vested stock options and restricted stock units is expected to be recognized over a weighted average period of 2.1 years and 2.0 years, respectively.

ASC 718 requires that cash flows relating to the benefits of tax deductions in excess of recognized compensation cost be reported as financing cash flow, rather than as an operating cash flow. The Company recognized excess tax benefits of \$2.6 million, \$3.5 million, and \$8.0 million for the years ended December 31, 2014, 2013 and 2012, respectively.

**Stock Options**

In 2014, 2013, and 2012 the Company granted stock options for 454,161, 604,296, and 625,942 common shares respectively, to executive officers, directors and employees as compensation for service. The Company's outstanding stock options vest as follows: 50 percent after two years and the remaining 50 percent after three years. Stock options granted in 2014, 2013, and 2012 have a contractual term of ten years. The stock options are subject to forfeiture should these employees terminate their employment with the Company for certain reasons prior to vesting in their awards, or the occurrence of certain other events such as termination with cause. The exercise price of these stock options is based on closing market price of our common stock on the date of grant. Compensation expense is recorded on an accelerated basis over the awards' vesting periods.

In December 2013, the board of directors approved a two-for-one stock split. In accordance with the Company's Amended and Restated 2008 Incentive Plan, the compensation committee of the board of directors elected to increase the number of unexercised stock options. The increase in the number of options did not result in any incremental fair value or compensation cost.

In November 2012, the board of directors approved a special cash dividend of \$1.00 per share (amount reflects the stock split announce in December 2013). In accordance with the Company's Amended and Restated 2006 Incentive Plan, the compensation committee of the board of directors selected a \$1.00 reduction to the exercise price for the 2,563,856 unexercised stock options. The adjustment to the exercise price did not result in any incremental fair value or compensation cost.

Table of Contents**KAPSTONE PAPER AND PACKAGING CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

(\$ in thousands, except share and per share amounts)

**12. Stock-Based Compensation (Continued)**

A summary of information related to stock options is as follows (amounts restated for the 2013 stock split):

	Options	Weighted Average Exercise Price	Weighted Average Remaining Life (Years)	Intrinsic Value (dollars in thousands)
<b>Outstanding at December 31, 2011</b>	4,947,748	\$ 3.93		
Granted	625,942	9.88		
Exercised	(2,989,582)	2.98		
Lapsed (forfeited or cancelled)	(20,252)	8.24		
<b>Outstanding at December 31, 2012</b>	2,563,856	5.46		
Granted	604,296	14.53		
Exercised	(616,406)	3.51		
Lapsed (forfeited or cancelled)	(37,364)	9.43		
<b>Outstanding at December 31, 2013</b>	2,514,382	8.05		
Granted	454,161	30.42		
Exercised	(183,130)	5.74		
Forfeited	(26,107)	16.85		
<b>Outstanding at December 31, 2014</b>	2,759,306	\$ 11.81	6.8	\$ 48,799
Exercisable at December 31, 2014	1,494,206	\$ 5.88	5.5	\$ 35,017

The total intrinsic value of options exercised during 2014, 2013, and 2012 was \$4.5 million, \$10.5 million, and \$23.4 million, respectively.

The weighted average fair value of the Company stock options granted in 2014, 2013 and 2012 was \$10.39, \$5.58, and \$5.19, respectively. The fair value of awards granted in 2014, 2013 and 2012 was \$4.7 million, \$3.4 million, and \$3.2 million, respectively. The fair value was calculated using the Black-Scholes option-pricing model based on the market price at the grant date and the weighted average assumptions specific to the underlying options. Beginning in 2013, the expected life used by the Company is based on the historical average life of stock option awards. In 2012, the Company used the "simplified method", defined in SEC Staff Accounting Bulletin ("SAB") No. 107, to determine the expected life assumption for all of its options. The expected volatility assumption is based on the volatility of the Company's common stock from the same time period as the expected term of the stock options. The risk-free interest rate was selected based upon yields of U.S. Treasury issues with a term similar to the expected life of the stock options.



Table of Contents**KAPSTONE PAPER AND PACKAGING CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

(\$ in thousands, except share and per share amounts)

**12. Stock-Based Compensation (Continued)**

The assumptions utilized for determining the fair value of stock options awarded during the years 2014, 2013 and 2012 are as follows:

	December 31,		
	2014	2013	2012
KapStone Stock Options Black-Scholes assumptions (weighted average):			
Expected volatility	39.92%	49.39%	56.47%
Expected life (years)	4.32	4.00	5.99
Risk-free interest rate	1.35%	0.63%	1.10%
Expected dividend yield	%	%	%

**Restricted Stock**

In 2014, 2013, and 2012, the Company granted restricted stock units of 161,418, 233,544, and 250,382 to executive officers, directors, and employees as compensation for service. These are restricted as to transferability until they vest three years from the grant date. These restricted shares are subject to forfeiture should these employees terminate their employment with the Company for certain reasons prior to vesting in their awards, or the occurrence of certain other events. The value of these restricted shares is based on the closing market price of the Company's common stock on the date of grant and compensation expense is recorded on a straight-line basis over the awards' vesting periods.

In November 2012, the compensation committee of the board of directors adopted a resolution directing that the Restricted Stock Unit Grant Agreements pertaining to the RSUs awarded on May 27, 2010 be amended to reflect an accelerated vesting date of November 28, 2012, except for the Company's Chief Operating Officer and certain grantees who attained the age of 65 years on or prior to November 28, 2012. Accordingly, 143,754 restricted stock units vested on November 28, 2012 (amount reflects restatement for the stock split declared in December 2013).

Table of Contents**KAPSTONE PAPER AND PACKAGING CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

(\$ in thousands, except share and per share amounts)

**12. Stock-Based Compensation (Continued)**

The following table summarizes non-vested restricted stock amounts and activity (amounts in 2013, 2012, and 2011 are restated for the stock split):

	Units	Weighted Average Grant Price
<b>Outstanding at December 31, 2011</b>	992,790	\$ 4.61
Granted	250,382	9.88
Vested	(577,322)	2.81
Forfeited	(14,326)	7.77
<b>Outstanding at December 31, 2012</b>	651,524	\$ 8.18
Granted	233,544	14.44
Vested	(181,578)	5.73
Forfeited	(16,122)	10.19
<b>Outstanding at December 31, 2013</b>	687,368	\$ 10.91
Granted	161,418	30.44
Vested	(248,293)	9.00
Forfeited	(12,426)	15.25
<b>Outstanding at December 31, 2014</b>	588,067	\$ 16.98

The fair value of awards granted in 2014, 2013 and 2012 was \$4.9 million, \$3.4 million, and \$2.5 million, respectively. The fair value of awards vested in 2014, 2013 and 2012 was \$2.2 million, \$1.0 million, and \$1.6 million, respectively.

**13. Commitments and Contingencies****Commercial Commitments**

The Company's commercial commitments as of December 31, 2014 represent commitments not recorded on the balance sheet, but potentially triggered by future events, primarily consist of letters of credit to provide security for certain transactions and operating leases as requested by third parties. The Company had \$4.3 million and \$4.7 million of these commitments as of December 31, 2014 and 2013, respectively, with all expiring in 2015 if not renewed. No amounts have been drawn under these letters of credit.

**Legal claims**

We are from time to time subject to various administrative and legal investigations, claims and proceedings incidental to our business, including environmental and safety matters, labor and employment matters, personal injury claims, contractual disputes and taxes. We establish reserves for claims and proceedings when it is probable that liabilities exist and where reasonable estimates can be made. We also maintain insurance that may limit our financial exposure for defense costs, as well as liability, if any, for claims covered by the insurance (subject also to deductibles and self-insurance amounts). While any investigation, claim or proceeding has an element of uncertainty, and we cannot



Table of Contents**KAPSTONE PAPER AND PACKAGING CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

(\$ in thousands, except share and per share amounts)

**13. Commitments and Contingencies (Continued)**

predict or assure the outcome of any claim or proceeding involving the Company, we believe the outcome of any pending or threatened claim or proceeding (other than those that cannot be assessed due to their preliminary nature), or all of them combined, will not have a material adverse effect on our results of operations, cash flows or financial condition.

The Company's subsidiary, Longview, is a potentially responsible party under the Comprehensive Environmental Response, Compensation and Liability Act ("CERCLA") with respect to the Lower Duwamish Waterway Superfund Site in the State of Washington (the "Site"). The U.S. Environmental Protection Agency ("EPA") asserts that the Site is contaminated as a result of discharges from various businesses and government entities located along the Lower Duwamish Waterway, including a corrugated converting plant owned and operated by Longview. In November 2014, the EPA issued a Record of Decision ("ROD") for the Site. The ROD includes a selected remedy for the Site. In the ROD, EPA states that the total estimated net present value costs (discounted at 2.3%) for the selected remedy are \$342 million. At least 40 potentially responsible parties, including Longview, have entered into an Allocation Agreement. Pursuant to the Allocation Agreement, the parties will attempt to determine each party's portion of the cost to remediate the site. The allocation process is not expected to be completed until 2017. Based on available information provided to the Company to date, the Company cannot reasonably estimate its potential liability.

**Operating Leases**

The Company leases space for twelve of its corrugated manufacturing plants with the majority of space leased through 2032. The leases include a provision for a one percent rent increase beginning in 2020.

**Future minimum rentals under non-cancellable leases**

The following represents the Company's future minimum rental payments due under non-cancellable operating leases that have initial or remaining lease terms in excess of one year as of the following years:

<b>Years Ended December 31,</b>	
2015	\$ 12,219
2016	15,708
2017	13,365
2018	8,273
2019	7,463
Thereafter	32,199
<b>Total</b>	<b>\$ 89,227</b>

The Company's rental expense under operating leases amounted to \$16.9 million, \$14.9 million, and \$12.0 million for the years ended December 31, 2014, 2013 and 2012, respectively.

Table of Contents**KAPSTONE PAPER AND PACKAGING CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

(\$ in thousands, except share and per share amounts)

**13. Commitments and Contingencies (Continued)****Purchase Obligation**

In conjunction with the 2008 Charleston Kraft Division acquisition, the Company entered into a long-term fiber supply agreement with MeadWestvaco Corporation ("MWV"), MWV's rights and obligations under the long-term fiber supply agreement were assigned to Plum Creek in December 2013. Pursuant to the agreement, the Company's North Charleston mill will purchase approximately 25 percent of its pine pulpwood and 60 percent of its saw timber requirements for a period of 15 years and expiring in 2023. The purchases are based on market prices and are accounted for as raw fiber materials. The Company's North Charleston mill purchased approximately \$40.0 million, \$35.6 million, and \$42.9 million of materials in accordance with the agreement for years ended December 31, 2014, 2013 and 2012, respectively.

**Limited Partnership Investments**

The KapStone Defined Benefit Pension Plan invests in various limited partnership investments in accordance with their stated investment policies. As of December 31, 2014, the plan had unfunded commitments to contribute capital to limited partnerships totaling \$4.6 million.

**14. Net income per share**

The Company's basic and diluted net income per share is calculated as follows:

	Years Ended December 31,		
	2014	2013	2012
Net income	\$ 171,915	\$ 127,338	\$ 62,505
Weighted-average number of common shares for basic net income per share	95,900,179	95,258,756	93,426,912
Incremental effect of dilutive common stock equivalents:			
Unexercised stock options	1,207,903	1,038,293	1,489,656
Unvested restricted stock awards	351,102	442,433	536,310
Weighted-average number of shares for diluted net income per share	97,459,184	96,739,482	95,452,878
Net income per share basic	\$ 1.79	\$ 1.34	\$ 0.67
Net income per share diluted	\$ 1.76	\$ 1.32	\$ 0.65

A total of 355,132 and 2,974 weighted average unexercised stock options were outstanding at December 31, 2014, and 2013, respectively, but were not included in the computation of diluted net income per share because the awards were anti-dilutive.

On December 11, 2013, the board of directors declared a two-for-one stock split in the form of a stock dividend on the Company's common stock, which was distributed on January 7, 2014. All shares and earnings per share amounts for 2013 and 2013 have been restated to reflect this change.

Table of Contents**KAPSTONE PAPER AND PACKAGING CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

(\$ in thousands, except share and per share amounts)

**15. Segment Information**

The Company has one operating segment. The Company produces containerboard, corrugated products, and specialty paper which are sold to customers who convert our products into end-market finished products or internally to corrugating plants which produce a wide variety of products ranging from basic corrugated shipping containers to specialized packaging.

The Company's identification of one operating segment is based on financial information regularly evaluated by the chief operating decision maker in determining resource allocation and assessing performance, in accordance with ASC 805, *Segment Reporting*.

Net sales for the years ended December 31, 2014, 2013, and 2012 are as follows:

Net sales by product line:	Years Ended December 31,		
	2014	2013	2012
Containerboard / Corrugated products	\$ 1,463,670	\$ 1,108,545	\$ 714,085
Specialty paper	741,601	551,931	428,663
Other	95,649	87,686	73,889
Total	\$ 2,300,920	\$ 1,748,162	\$ 1,216,637

Net sales by location:	Years Ended December 31,		
	2014	2013	2012
To customers located in the United States	\$ 1,847,531	\$ 1,398,326	\$ 942,706
Export sales to foreign based customers	453,389	349,836	273,931
Total	\$ 2,300,920	\$ 1,748,162	\$ 1,216,637

For the years ended December 31, 2014, 2013, and 2012 the Company had other sales of \$95.6 million, \$87.7 million, and \$73.9 million, respectively, from lumber, shaft horsepower generated by our cogeneration facility, and other energy sales.

No foreign country accounted for more than 10 percent of consolidated net sales in 2014, 2013, or 2012.

All long-lived assets are located within the United States.

**16. Quarterly Financial Information (Unaudited)**

The following tables set forth the historical unaudited quarterly financial data for 2014 and 2013. The information for each of these periods has been prepared on the same basis as the audited consolidated financial statements and, in our opinion, reflects all adjustments consisting only of normal

Table of Contents**KAPSTONE PAPER AND PACKAGING CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

(\$ in thousands, except share and per share amounts)

**16. Quarterly Financial Information (Unaudited) (Continued)**

recurring adjustments necessary to present fairly our financial results. Operating results for previous periods do not necessarily indicate results that may be achieved in any future period.

	Quarters Ended			
	March 31, 2014	June 30, 2014	September 30, 2014	December 31, 2014
<b>Fiscal 2014:</b>				
Net sales	\$ 548,952	\$ 590,449	\$ 598,106	\$ 563,413
Gross profit(1)	\$ 92,263	\$ 119,406	\$ 128,295	\$ 96,976
Operating income	\$ 58,118	\$ 85,313	\$ 94,162	\$ 62,338
Net income(2)	\$ 32,099	\$ 51,459	\$ 54,254	\$ 34,103
Net income per share:				
Basic	\$ 0.34	\$ 0.54	\$ 0.57	\$ 0.36
Diluted	\$ 0.33	\$ 0.53	\$ 0.56	\$ 0.35

- (1) Gross profit is defined as net sales less cost of sales, depreciation and amortization, freight, and distribution expenses. Gross profit includes planned maintenance outage costs of \$14.8 million, \$5.2 million, \$ 5.2 million, and \$10.9 million in the quarters ended March 31, June 30, September 30 and December 31, 2014, respectively.
- (2) Net income includes a loss on debt extinguishment of \$3.0 million and \$2.6 million for the quarters ended September 30 and December 31, 2014, respectively.

	Quarters Ended			
	March 31, 2013	June 30, 2013	September 30, 2013(1)	December 31, 2013(1)
<b>Fiscal 2013:</b>				
Net sales	\$ 319,813	\$ 326,321	\$ 538,603	\$ 563,425
Gross profit(2)	\$ 49,723	\$ 55,466	\$ 118,056	\$ 106,580
Operating income	\$ 30,797	\$ 34,590	\$ 80,695	\$ 73,806
Net income(3)	\$ 18,459	\$ 20,991	\$ 44,414	\$ 43,474
Net income per share(4):				
Basic	\$ 0.19	\$ 0.22	\$ 0.47	\$ 0.45
Diluted	\$ 0.19	\$ 0.22	\$ 0.46	\$ 0.45

- (1) Results of the Longview acquisition are included above since July 18, 2013.
- (2) Gross profit is defined as net sales less cost of sales, depreciation and amortization, freight, and distribution expenses. Gross profit includes planned maintenance outage costs of \$10.5 million in the quarter ended December 31, 2013.
- (3)

Edgar Filing: KAPSTONE PAPER & PACKAGING CORP - Form 10-K

Includes \$5.0 million for a reversal of a tax reserve relating to an uncertain tax position in the quarter ended December 31, 2013.

(4)

Net income per share, for all periods, has been restated for the stock split declared in December 2013.

F-43

---