GEORGIA PACIFIC CORP
Form 10-Q/A
May 03, 2001

SECURITIES AND EXCHANGE COMMISSION

Washington, D. C. 20549

FORM 10-Q/A
AMENDMENT NO. 1

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

For the quarterly period ended March 31, 2001

or

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

For the transition period from ______ to ______

Commission File Number 1 - 3506

GEORGIA-PACIFIC CORPORATION
(Exact Name of Registrant as Specified in its Charter)

GEORGIA 93-0432081
(State of Incorporation) (IRS Employer Id. Number)

133 PEACHTREE STREET, N.E., ATLANTA, GEORGIA 30303
(Address of Principal Executive Offices)

(404) 652 - 4000
(Telephone Number of Registrant)

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 and Exchange Act of 1934 during the preceding 12 months and (2) has been subject to such filing requirements for the past 90 days. Yes __X__ No _____

As of the close of business on April 30, 2001, Georgia-Pacific Corporation had 225,915,912 shares of Georgia-Pacific Group Common Stock outstanding and 80,607,630 shares of The Timber Company Common Stock outstanding.

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Item 1 is hereby restated to amend Note 11 to update to March 31, 2001 certain information provided as of December 30, 2000.

PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

CONSOLIDATED STATEMENTS OF OPERATIONS (Unaudited)
Georgia-Pacific Corporation and Subsidiaries

	First Quarter	
(In millions, except per share amounts)	2001	2000
Net sales	$ 6,365	$ 5,564
Costs and expenses		
Cost of sales, excluding depreciation, depletion and cost of timber harvested shown below	4,951	4,170
Selling and distribution	525	368
Depreciation, depletion, amortization and cost of timber harvested	395	265
General and administrative	318	239
Interest	321	145
Total costs and expenses	6,510	5,187
(Loss) income before income taxes, extraordinary item and accounting change	(145)	377
Benefit (provision) for income taxes	31	(143)
(Loss) income before extraordinary item and accounting change	(114)	234
Extraordinary loss from early retirement of debt, net of taxes	(12)	-
Cumulative effect of accounting change, net of taxes	11	-
Net (loss) income	$ (115)	$ 234
Georgia-Pacific Group		
(Loss) income before extraordinary item and accounting change	$ (136)	$ 194

Extraordinary loss, net of taxes	(12)	-
Cumulative effect of accounting change, net of taxes	11	-
Net (loss) income	$ (137)	$ 194
Basic per share:		
(Loss) income before extraordinary item and accounting change	$ (0.60)	$ 1.13
Extraordinary loss, net of taxes	(0.05)	-
Cumulative effect of accounting change, net of taxes	0.04	-
Net (loss) income	$ (0.61)	$ 1.13

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Diluted per share:		
(Loss) income before extraordinary item and accounting change	$ (0.60)	$ 1.11
Extraordinary loss, net of taxes	(0.05)	-
Cumulative effect of accounting change, net of taxes	0.04	-
Net (loss) income	$ (0.61)	$ 1.11
Average number of shares outstanding:		
Basic	225.4	171.8
Diluted	225.4	174.8
The Timber Company		
Net income	$ 22	$ 40
Basic and diluted net income per common share	$ 0.27	$ 0.49
Average number of shares outstanding:		
Basic	80.4	82.3
Diluted	81.2	82.5

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

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CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)
Georgia-Pacific Corporation and Subsidiaries

	First quarter	
(In millions)	2001	2000
Cash flows from operating activities		
Net (loss) income	$ (115)	$ 234
Adjustments to reconcile net income to cash provided by operations:		
Cumulative effect of accounting change, net of taxes	(11)	-
Depreciation, depletion and amortization	362	226
Deferred income taxes	8	(4)
Loss (gain) on disposal of assets, net	41	(34)
Change in working capital	(137)	(183)
Other	35	27
Cash provided by operations	183	266
Cash flows from investing activities		
Property, plant and equipment investments	(192)	(182)
Timber and timberland purchases	(37)	(59)
Acquisitions	(71)	(1)
Net proceeds from sales of assets	605	25
Other	(19)	(7)
Cash provided by (used for) investing activities	286	(224)
Cash flows from financing activities		
Repayments of long-term debt	(837)	(21)
Additions to long-term debt	1,272	10
Fees paid to issue debt	(15)	-
Net (decrease) increase in short-term debt	(867)	73
Stock repurchases	-	(71)
Cash dividends paid	(48)	(42)
Proceeds from option plan exercises	29	3

Cash used for financing activities	(466)	(48)
Increase (decrease) in cash	3	(6)
Balance at beginning of period	40	25
Balance at end of period	$ 43	$ 19

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

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CONSOLIDATED BALANCE SHEETS (Unaudited)
Georgia-Pacific Corporation and Subsidiaries

(In millions, except shares and per share amounts)	March 31, 2001	December 30, 2000
ASSETS		
Current assets		
Cash	$ 43	$ 40
Receivables, less allowances of $35 and $34, respectively	2,697	2,705
Inventories	2,839	2,895
Deferred income tax assets	182	176
Other current assets	481	472
Total current assets	6,242	6,288
Timber and timberlands, net	1,296	1,293
Property, plant and equipment		
Land, buildings, machinery and equipment, at cost	20,645	21,223
Accumulated depreciation	(9,572)	(9,421)
Property, plant and equipment, net	11,073	11,802
Goodwill, net	9,047	8,985
Other assets	2,429	2,514
Total assets	$ 30,087	$ 30,882

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CONSOLIDATED BALANCE SHEETS (Unaudited) (Continued)

Georgia-Pacific Corporation and Subsidiaries

(In millions, except shares and per share amounts)	March 31, 2001	December 30, 2000
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities		
Bank overdrafts, net	$ 219	$ 293
Commercial paper and other short-term notes	1,902	2,695
Current portion of long-term debt	257	232
Accounts payable	1,522	1,520
Accrued compensation	292	436
Other current liabilities	1,036	906
Total current liabilities	5,228	6,082
Long-term debt, excluding current portion	13,023	12,627
Senior deferrable notes	863	863
Other long-term liabilities	3,053	3,027
Deferred income tax liabilities	2,366	2,561
Commitments and contingencies (Note 11)		
Shareholders' equity		
Common stock	183	182
Georgia-Pacific Group, par value $.80; 400,000,000 shares authorized; 225,393,000 and 224,844,000 shares issued		
The Timber Company, par value $.80; 250,000,000 shares authorized; 94,814,000 and 94,571,000 shares issued		
Treasury stock, at cost	(330)	(330)

14,387,000 shares of The Timber Company common stock		
Additional paid-in capital	2,464	2,427
Retained earnings	3,300	3,463
Long-term incentive plan deferred compensation	(4)	(4)
Accumulated other comprehensive loss	(59)	(16)
Total shareholders' equity	5,554	5,722
Total liabilities and shareholders' equity	$ 30,087	$ 30,882

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

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CONSOLIDATED STATEMENTS OF COMPREHENSIVE (LOSS) INCOME (Unaudited)
Georgia-Pacific Corporation and Subsidiaries

	First quarter	
(In millions)	2001	2000
Net (loss) income	$ (115)	$ 234
Other comprehensive income (loss) before tax:		
Foreign currency translation adjustments	(26)	(1)
Derivative instruments	(30)	-
Minimum pension liability adjustment	1	-
Income tax expense related to items of other comprehensive income	12	-
Comprehensive (loss) income	$ (158)	$ 233

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

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)
GEORGIA-PACIFIC CORPORATION
March 31, 2001

1. PRINCIPLES OF PRESENTATION AND ACCOUNTING POLICIES. The consolidated financial statements include the accounts of Georgia-Pacific Corporation and subsidiaries (the "Corporation"). All significant intercompany balances and transactions are eliminated in consolidation. The interim financial information included herein is unaudited; however, such information reflects all adjustments which are, in the opinion of management, necessary for a fair presentation of the Corporation's financial position, results of operations, and cash flows for the interim periods. All such adjustments are of a normal, recurring nature. Certain 2000 amounts have been reclassified to conform with the 2001 presentation. These consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Corporation's annual report on Form 10-K for the fiscal year ended December 30, 2000.

On December 16, 1997, shareholders of the Corporation approved the creation of two classes of common stock intended to reflect separately the performance of the Corporation's manufacturing and timber businesses. The Corporation's manufacturing and timber businesses are referred to hereinafter as the "Georgia-Pacific Group" and "The Timber Company", respectively. The Georgia-Pacific Group's and The Timber Company's combined financial information is presented in Note 12.

During the fourth quarter of 2000, the Corporation implemented EITF 00-10, *"Accounting for Shipping and Handling Fees and Costs"*. EITF 00-10 requires that entities disclose costs incurred related to shipping and handling that are not included in cost of sales. The Corporation currently classifies certain shipping and handling costs as selling and distribution expenses. Shipping and handling costs included in selling and distribution expenses were $187 million and $116 million for the first quarter ended March 31, 2001 and April 1, 2000, respectively.

2. PROVISION FOR INCOME TAXES. The effective tax rate used to calculate the benefit (provision) for income taxes was 21% in 2001 and 38% in 2000. The effective tax rate in 2001 was different from statutory rates primarily because of nondeductible goodwill amortization expense associated with business acquisitions. In 2000, the effective tax rate differed from the statutory rate, primarily because of increased state tax credits and increased utilization of foreign sales corporation tax benefits, which more than offset nondeductible goodwill amortization expense associated with business acquisitions.

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3. EARNINGS PER SHARE. Basic earnings per share is computed based on net income and the weighted average number of common shares outstanding. Diluted earnings per share reflect the assumed issuance of common shares under long-term incentive stock option and stock purchase plans and pursuant to the terms of the 7.5% Premium Equity Participating Security Units ("PEPS Units"). The computation of diluted earnings per share does not assume conversion or exercise of

securities that would have an antidilutive effect on earnings per share. Amounts are computed for each class of common stock based on the separate earnings attributed to each of the respective businesses.

The following table provides earnings and per share data for Georgia-Pacific Group and The Timber Company for 2001 and 2000.

(In millions, except per share amounts)	First Quarter 2001	First Quarter 2000
Georgia-Pacific Group		
Basic and diluted (loss) income available to shareholders (numerator):		
(Loss) income before extraordinary item and accounting change	$ (136)	$ 194
Extraordinary loss, net of taxes	(12)	-
Cumulative effect of accounting change	11	-
Net (loss) income	$ (137)	$ 194
Shares (denominator):		
Average shares outstanding	225.4	171.8
Dilutive securities:		
Options	-	3.0
Total assuming conversion	225.4	174.8
Basic per share:		
(Loss) income before extraordinary item and accounting change	$ (0.60)	$ 1.13
Extraordinary loss, net of taxes	(0.05)	-
Cumulative effect of accounting change, net of taxes	0.04	-
Net (loss) income	$ (0.61)	$ 1.13
Diluted per share:		
(Loss) income before extraordinary item and accounting change	$ (0.60)	$ 1.11
Extraordinary loss, net of taxes	(0.05)	-
Cumulative effect of accounting change, net of taxes	0.04	-

Net (loss) income	$ (0.61)	$ 1.11

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	The Timber Company	
Basic and diluted income available to shareholders (numerator):		
Net income	$ 22	$ 40
Shares (denominator):		
Average shares outstanding	80.4	82.3
Dilutive securities:		
Options	0.8	0.2
Total assuming conversion	81.2	82.5
Basic and diluted per share amounts		
Net income	$ 0.27	$ 0.49

4. SUPPLEMENTAL DISCLOSURES - STATEMENTS OF CASH FLOWS. The cash impact of interest and income taxes is reflected in the table below. The effect of foreign currency exchange rate changes on cash was not material in either period.

	First quarter	
(In millions)	2001	2000
Total interest costs	$ 323	$ 147
Interest capitalized	(2)	(2)
Interest expense	$ 321	$ 145
Interest paid	$ 303	$ 114

Income tax (refunds received) paid, net	$	(82)	$	27

5. INVENTORY VALUATION. Inventories include costs of materials, labor, and plant overhead. The Corporation uses the dollar value method for computing LIFO inventories. The major components of inventories were as follows:

(In millions)		March 31, 2001		December 30, 2000
Raw materials	$	597	$	655
Finished goods		1,873		1,868
Supplies		538		550
LIFO reserve		(169)		(178)
Total inventories	$	2,839	$	2,895

6. DIVESTITURES, ACQUISITIONS AND UNUSUAL ITEMS. On March 30, 2001, the Corporation announced that it will permanently close its pulp mill and associated chemical plant at Bellingham, Washington. These operations had been temporarily closed since December 2000. The Bellingham pulp mill produced approximately 220,000 tons of pulp, including 135,000 tons of sulfite market pulp, and 260,000 tons of lignin annually. In connection with this closure the Corporation recorded liabilities totaling approximately $57 million for the write-off of assets, approximately $13 million for the termination of approximately 420 hourly and salaried employees and approximately $12 million for facility closure costs. Of the $82 million total liability, $78 million was charged to cost of sales, $3 million was charged to selling and distribution expense and $1 million was charged to general and administrative expenses. None of the reserves were used as of March 31, 2001.

* During the first quarter of 2001, the Corporation acquired the remaining ownership of two chemical joint ventures for approximately $26 million. The results of operations of these chemical businesses were consolidated with those of the Corporation beginning in February 2001. The Corporation has accounted for these acquisitions using the purchase method to record a new cost basis for assets acquired and liabilities assumed.

* At the end of November 2000, the Corporation completed a tender offer pursuant to which it purchased each outstanding share of common stock of Fort James Corporation ("Fort James") for $29.60 per share in cash and 0.2644 shares of Georgia-Pacific Group common stock. The Corporation is paying cash and issuing Georgia-Pacific Group shares as the untendered Fort James

shares are delivered to the Corporation's exchange agent for cancellation. Through March 31, 2001, the Corporation paid approximately $6,185 million in cash and issued approximately 53.9 million shares of Georgia-Pacific Group common stock valued at $1,484 million for such shares. The fair value of the Georgia-Pacific Group common shares was determined based on the average trading prices of Georgia-Pacific Group common stock for the two trading days before and after July 16, 2000 (the announcement of the Fort James acquisition). The Corporation expects to pay an additional $10 million in cash and issue approximately 91,000 shares valued at $3 million for Fort James common stock that had not been tendered as of March 31, 2001. In addition, the Corporation assumed $3.3 billion of Fort James debt in the acquisition.

Fort James' results of operations were consolidated with those of the Corporation beginning in the fiscal month of December 2000. The Corporation has accounted for this business combination using the purchase method to record a new cost basis for assets acquired and liabilities assumed. The allocation of the purchase price and acquisition costs to the assets acquired and liabilities assumed is preliminary as of March 31, 2001, and is subject to change pending finalization of studies of fair value and the finalization of management's plans to restructure certain operations. The difference between the purchase price and the fair value of the assets acquired and liabilities assumed was recorded as goodwill and is being amortized over 40 years. The preliminary allocation of net cash paid for the Fort James acquisition as of March 31, 2001 is summarized as follows:

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In millions		
Current assets	$	1,749
Property, plant and equipment		4,630
Other noncurrent assets		801
Goodwill		6,779
Liabilities		(6,173)
Common stock issued and value of stock options Converted		(1,601)
Net cash paid for Fort James	$	6,185

In connection with the acquisition of Fort James, the Corporation recorded liabilities totaling approximately $53 million for employee termination costs relating to approximately 520 hourly and salaried employees. During 2000, no employees were terminated and none of this reserve was used. During 2001, approximately 65 employees were terminated and approximately $16 million of the reserve was used to pay termination benefits. The Corporation has not finalized its plans for manufacturing and distribution activities. Finalization of these plans may result in additional liabilities recorded as part of the purchase price or charges to earnings. The following table provides a rollforward of the employee separation reserve from December 30, 2000 through March 31, 2001:

In millions

Type of Cost	Balance Dec. 30, 2000	Additions	Usage	Reversal of Reserves	Balance March 31, 2001
Employee separation	$ 30	$ 23	$ (16)	$ -	$ 37

The following unaudited pro forma financial data has been prepared assuming that the acquisition of Fort James and related financings were consummated on January 2, 2000. This pro forma financial data is presented for informational purposes and is not indicative of the operating results that would have occurred had the acquisition been consummated on January 2, 2000, nor does it include adjustments for expected synergies, cost savings or consistent application of accounting methods. Accordingly, this pro forma data is not necessarily indicative of future operations.

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In millions, except per share amounts	Quarter Ended April 1, 2000 Pro forma
Georgia-Pacific Corporation:	
Net sales	$ 7,192
(Loss) income before extraordinary item and accounting change	220
Net (loss) income	220
Georgia-Pacific Group data:	
Net sales	7,154
(Loss) income before extraordinary item and	180

accounting change	
Net (loss) income	180
Basic per share from (loss) income before	
extraordinary item and accounting change	0.80
Diluted per share from (loss) income before	
extraordinary item and accounting change	0.79
Basic (loss) earnings per share	0.80
Diluted (loss) earnings per share	0.79

The Timber Company's results of operations are not impacted by the Fort James transaction.

* In connection with the acquisition of Fort James and pursuant to a consent decree with the U. S. Department of Justice, the Corporation sold a portion of its away-from-home tissue manufacturing operations (formerly Georgia-Pacific Tissue) to Svenska Cellulosa Aktiebolaget SCA for approximately $850 million . The sale was completed on March 2, 2001, with net proceeds of approximately $582 million used to repay debt.

* During 2000, the Corporation announced the closure of the Grand Rapids East, Mich., gypsum plant and the Kalamazoo, Mich., paper mill. In connection with these closures, the Corporation recorded a charge to earnings totaling $7 million for the termination of approximately 325 salaried and hourly positions, $25 million for the write-off of assets and $12 million for facility closing costs. During 2000, approximately 284 employees were terminated and an additional 34 employees were terminated during the first quarter of 2001. The following table provides information related to these charges:

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In millions Type of Cost	Liability Balance at Dec. 30, 2000	Usage	Liability Balance at March 31, 2000
Write-off of assets	$ 2	$ -	$ 2
Employee separation	7	(5)	2
Facility closing costs	10	-	10
Total	$ 19	$ (5)	$ 14

* During the first quarter of 2000, the Corporation sold certain containerboard and packaging assets resulting in a pre-tax gain of $24.4 million ($15.3 million after tax, or $0.09 diluted earnings per Georgia-Pacific Group share).

* Also during the first quarter of 2000, the Corporation contributed certain containerboard and packaging assets with a net book value of $34 million to a joint venture. In exchange for these assets, the Corporation will retain a 52% interest in the joint venture. This investment in the joint venture is accounted for under the equity method.

* On July 18, 2000, the Corporation signed a definitive agreement to merge The Timber Company with and into Plum Creek Timber Company ("Plum Creek"). Under the agreement, The Timber Company shareholders will receive 1.37 shares of Plum Creek stock for each share of The Timber Company stock. This transaction, which includes the assumption by Plum Creek of approximately $621 million of debt allocated to The Timber Company, is valued at approximately $3.6 billion. Plum Creek will assume a 10-year wood supply agreement between Georgia-Pacific Group and The Timber Company. The transaction is subject to approval by the shareholders of both Plum Creek and The Timber Company, receipt of a ruling from the Internal Revenue Service (the "Service") that the transaction will be tax-free to the Corporation and to the shareholders of The Timber Company, and receipt of an opinion from counsel that the merger will qualify as a tax-free reorganization. The transaction is also subject to the satisfaction of customary closing conditions. The Corporation will treat The Timber Company as a discontinued operation once the significant contingencies surrounding the transaction are resolved.

  While discussions with the Service continue, it is uncertain whether the Service will issue the requested ruling. In the event that such a ruling is not issued, the Corporation will continue discussions with Plum Creek to determine if an acceptable alternate structure is feasible. In the event no such alternate structure is agreed upon, The Timber Company will be spun off to its shareholders, which will result in it being an independent, publicly-traded company.

* In connection with the acquisition of Unisource Worldwide, Inc. ("Unisource") at the end of the second quarter of 1999, the Corporation recorded liabilities totaling approximately $50 million for employee termination (relating to approximately 1,170 hourly and salaried employees) and relocation costs, and $22 million for closing costs of 48 facilities. The balance of these restructuring reserves at December 30, 2000 was $8 million. During 2001, approximately 151 employees were terminated as part of this program. The following table provides a rollforward of the reserve for restructuring from December 30, 2000 through March 31, 2001:

In millions

Type of Cost	Balance Dec. 30, 2000	Additions	Usage	Reversal of Reserves	Balance March 31, 2001
Employee separation	$ 3	$ -	$ (2)	$ -	$ 1
Facility closing costs	5	-	(2)	-	3
Total	$ 8	$ -	$ (4)	$ -	$ 4

7. DEBT. At March 31, 2001, the Corporation's debt was $15.40 billion, $14.78 billion of which was allocated to the Georgia-Pacific Group and $621 million of which was allocated to The Timber Company. The debt allocated to each group bears interest at a rate equal to the weighted average interest rate of the Corporation's total debt, calculated on a quarterly basis. At March 31, 2001, the weighted average interest rate on the Corporation's total debt, excluding senior deferrable notes, was 6.89% including outstanding interest rate exchange agreements. Each group's debt increases or decreases by the amount of any cash provided by or used for that group's operating activities, investing activities, dividend payments, share repurchases or issuances and other non-debt-related financing activities.

During the first quarter of 2001, the Corporation increased its accounts receivable secured borrowing program to $800 million and extended the program through October 2001. Additionally, the Corporation retained former Unisource agreements to sell up to $150 million of certain qualifying U.S. accounts receivable and up to CN$70 million of certain eligible Canadian accounts receivable. The Corporation increased the Canadian accounts receivable secured borrowing program to CN$95 million in the first quarter of 2001. The U.S. agreement expires in October 2001 and the Canadian agreement expires in May 2004. At March 31, 2001, approximately $860 million was outstanding under the Corporation's accounts receivable secured borrowing programs in the aggregate. The receivables outstanding under these programs and the corresponding debt are included as both "Receivables" and "Commercial paper and other short-term notes", respectively, on the accompanying balance sheets. All programs are accounted for as secured borrowings. As collections reduce previously pledged interests, new receivables may be pledged.

On March 15, 2001, the Corporation amended the restrictive covenants under its unsecured revolving credit facility (the "credit facility"). These amendments included increasing the maximum leverage ratio (funded indebtedness, excluding senior deferrable notes, to earnings before interest, taxes, depreciation and amortization ("EBITDA")) to 4.50 to 1.00 on March 31, 2001; 4.75 to 1.00 on June 30, 2001; 4.50 to 1.00 on September 29, 2001 and December 29, 2001; 4.25 to 1.00 on March 30, 2002; 4.00 to 1.00 on June 29, 2002 and thereafter. The restrictive covenants also require a minimum net worth that will change on a quarterly basis. The Corporation was in compliance with its debt covenants as of March 31, 2001. As of March 31, 2001, the temporary credit facility totaled $5,400 million with terms ranging from 6 to 18 months and the permanent credit facility totaled $3,750 million with a term of 5 years. As of March 31, 2001, $1,404 million of committed credit was available in excess of all borrowings outstanding under or supported by these credit facilities.

On March 15, 2001, the Corporation redeemed $300 million of its 6.234% Senior Notes Due March 15, 2011. The Corporation recorded an after-tax extraordinary loss of approximately $12 million related to this redemption during the 2001 first quarter, which was allocated to Georgia-Pacific Group. In addition, the Corporation had $300 million of swaps terminate on March 15, 2001 and $55 million of its 9.25% Senior Notes Due March 15, 2001 mature.

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In January 2001, the Corporation entered into several interest rate exchange agreements that effectively converted $1,500 million of floating rate obligations into fixed rate obligations. At March 31, 2001, the weighted average interest rate was 5.6% for the fixed rate obligations with an average effective interest rate of approximately 5.9%. These agreements have a weighted-average maturity of approximately 1.2 years as of March 31, 2001.

8. DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES. Effective December 31, 2000, the Corporation adopted Statement of Financial Accounting Standards No. 133, "*Accounting for Derivative Instruments and Hedging Activities,"* and, accordingly, recorded an after-tax cumulative effect of accounting change credit of $11 million. All derivatives are recognized on the balance sheet at their fair value. On the date the derivative contract is entered into, the Corporation designates the derivative as either (1) a fair value hedge, (2) a cash flow hedge, (3) the hedge of a net investment in a foreign operation or (4) a non-designated derivative instrument. The Corporation engages primarily in derivatives classified as cash flow hedges, and changes in the fair value of highly effective derivatives are recorded in accumulated other comprehensive (loss) income. The Corporation also participates in some derivatives that are classified as non-designated derivative instruments and a hedge in the net investment of the European operations. Changes in the fair value of the non-designated derivative instruments and any ineffectiveness in cash flow hedges are reported in current period earnings. The changes in fair value of the hedge in the net investment of the European operations are recorded in accumulated other comprehensive (loss) income.

The Corporation formally documents all relations between hedging instruments and the hedged items, as well as its risk-management objectives and strategy for undertaking various hedge transactions. The Corporation formally assesses, both at the hedge's inception and on an ongoing basis, whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in cash flows of the hedged items.

* Cash Flow Hedges:

The Corporation uses interest rate swap and foreign currency exchange agreements in the normal course of business to manage and reduce the risk inherent in interest rate and foreign currency fluctuations. Interest rate swap agreements are considered hedges of specific borrowings and differences paid and received under the swap arrangements are recognized as adjustments to interest expense. Such contracts had a total notional amount of $1,957 million at March 31, 2001.

The Corporation's international operations create exposure to foreign currency exchange rate risks. To manage these risks, the Corporation utilizes short-term foreign exchange contracts. As of March

31, 2001, the Corporation had outstanding foreign exchange contracts with notional amounts of $14 million to hedge firm and anticipated purchase commitments and firm sales commitments denominated in foreign currencies. A 10% change from the prevailing market rates of these foreign currencies would not have a material effect on the results of operations.

The Corporation also utilizes swap agreements to manage and reduce the risk inherent in market value fluctuations of certain commodities. These commodity swap agreements are designated as hedges of forecasted transactions included in fixed price sales contracts with customers. Amounts paid or received under these arrangements are recognized as adjustments to net sales. As of March 31, 2001, the Corporation had outstanding commodity swap cash flow hedges with notional amounts of $2.6 million with maturity periods of 2 months to 5 years.

With each type of cash flow hedge, the settlement of the forecasted transaction will result in the reclassification into earnings of gains and losses that are reported in accumulated other comprehensive (loss) income. As of March 31, 2001, approximately $2 million of deferred gains on derivative instruments included in accumulated other comprehensive loss are expected to be reclassified to earnings during the next twelve months.

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* Hedge of the net investment in a foreign operation:

At March 31, 2001, the Corporation had outstanding approximately $228 million (net of discount) of Euro-denominated bonds which were designated as a hedge against its net investment in Europe. The use of these derivative financial instruments allows the Corporation to reduce its overall exposure to exchange rate movements, since the gains and losses on these contracts substantially offset losses and gains on the assets, liabilities and transactions being hedged.

* Non-designated/ineffective derivative instruments:

The Corporation has certain derivative instruments that have been assessed as ineffective hedges or do not qualify for hedge accounting in accordance with SFAS No. 133. Certain commodity swap agreements have been assessed as ineffective due to the variance between the fixed price portion of the swap agreement and the fixed price offered to the customer. The fair value of these contracts at December 31, 2000 was $1.3 million (pre-tax) and is included in the cumulative effect of accounting change.

The Corporation also has two foreign currency interest rate swap agreements that were assumed as a result of the acquisition of Fort James. These agreements do not qualify for hedge accounting. Included in the cumulative effect of accounting change is a pre-tax loss of $1 million relating to the fair value of these agreements.

During 2000, the Corporation entered into a derivative agreement in connection with the sale of certain containerboard and packaging assets whereby the Corporation has guaranteed a certain margin on the buyer's production. This derivative agreement expires in 2005. This agreement does not qualify for hedge accounting because the buyer's production does not qualify as a hedged item in accordance with SFAS No. 133. The Corporation also entered into certain commodity swap agreements to offset the gain on the aforementioned derivative agreement. The net fair value of these derivative agreements was $17.3 million (pre-tax) at December 31, 2000 and is included in the cumulative effect of accounting change.

The Corporation's senior management establishes the parameters of the Corporation's financial risk, which have been approved by the Board of Directors . Hedging interest rate exposure through the use of swaps and options and hedging foreign exchange exposure through the use of forward contracts are specifically contemplated to manage risk in keeping with management's policy. Derivative instruments, such as swaps, forwards, options or futures, which are based directly or indirectly upon interest rates, currencies, equities and commodities, may be used by the Corporation to manage and reduce the risk inherent in price, currency and interest rate fluctuations.

The Corporation does not utilize derivatives for speculative purposes. Derivatives are transaction-specific so that a specific debt instrument, contract or invoice determines the amount, maturity and other specifics of the hedge. Counterparty risk is limited to institutions with long-term debt ratings of A or better.

9. LONG-TERM APPRECIATION PLAN. The Corporation reserved 2,600,000 stock appreciation rights ("SAR") for issuance under the 2001 Long-Term Appreciation Plan (the "LTAP"). The LTAP provides for the granting of SAR units to key employees of the Corporation. During the first quarter of 2001, the Corporation issued 1.4 million SAR units under the LTAP with at an exercise price of $29.47 per unit. The SAR exercise price was based on the underlying fair value of Georgia-Pacific Group common stock at the grant date. These SAR units vest over three years. Compensation expense for the SARs is based on the difference between the current fair market value of Georgia-Pacific Group common stock and the fair market value at the date of grant. As of March 31, 2000 no compensation expense was recorded.

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10. SHARE REPURCHASES. In November of 2000, the Corporation acquired Fort James (see Note 6). Through March 31, 2001, the Corporation has issued 21.5 million shares of Georgia-Pacific Group treasury stock and 32.4 million newly issued shares of Georgia-Pacific Group stock in exchange for outstanding common stock of Fort James. The Corporation does not hold any Georgia-Pacific Group stock in Treasury as of March 31, 2001. Effective with the agreement to dispose of The Timber Company (see Note 6), the Corporation is precluded from purchasing shares of The Timber Company Stock.

During the first quarter of 2000, Georgia-Pacific Group purchased on the open market approximately 1,414,000 shares of Georgia-Pacific Group common stock at an aggregate price of approximately $50 million ($35.48 average per share), all of which were held as treasury stock at April 1, 2000. During the first quarter of 2000, The Timber Company purchased on the open market approximately 1,075,000 shares of The Timber Company common stock at an aggregate price of approximately $25 million ($22.77 average per share). Of these repurchased shares, approximately 899,000 shares of The Timber Company common stock were held as treasury stock and approximately 176,000 shares were purchased during the first quarter of 2000 and settled after April 1, 2000.

11. COMMITMENTS AND CONTINGENCIES. The Corporation is a party to various legal proceedings incidental to its business and is subject to a variety of environmental and pollution control laws and regulations in all jurisdictions in which it operates. As is the case with other companies in similar industries, the Corporation faces exposure from actual or potential claims and legal proceedings involving environmental matters. Liability insurance in effect during the last several years provides only very limited coverage for environmental matters.

The Corporation is involved in environmental remediation activities at approximately 189 sites, both owned by the Corporation and owned by others, where it has been notified that it is or may be a potentially responsible party under the Comprehensive Environmental Response, Compensation and Liability Act or similar state "superfund" laws. Of the known sites in which it is involved, the Corporation estimates that approximately 46% are being investigated, approximately 28% are being remediated and approximately 26% are being monitored (an activity that occurs after either site investigation or remediation has been completed). The ultimate costs to the Corporation for the investigation, remediation and monitoring of many of these sites cannot be predicted with certainty, due to the often unknown magnitude of the pollution or the necessary cleanup, the varying costs of alternative cleanup methods, the amount of time necessary to accomplish such cleanups, the evolving nature of cleanup technologies and governmental regulations, and the inability to determine the Corporation's share of multiparty cleanups or the extent to which contribution will be available from other parties. The Corporation has established reserves for environmental remediation costs for these sites in amounts that it believes are probable and reasonably estimable. Based on analysis of currently available information and previous experience with respect to the cleanup of hazardous substances, the Corporation believes it is reasonably possible that costs associated with these sites may exceed current reserves by amounts that may prove insignificant or that could range, in the aggregate, up to approximately $154 million. This estimate of the range of reasonably possible additional costs is less certain than the estimates upon which reserves are based, and in order to establish the upper limit of such range, assumptions least favorable to the Corporation among the range of reasonably possible outcomes were used. In estimating both its current reserve for environmental remediation and the possible range of additional costs, the Corporation has not assumed it will bear the entire cost of remediation of every site to the exclusion of other known potentially responsible parties who may be jointly and severally liable. The ability of other potentially responsible parties to participate has been taken into account, based generally on the parties' financial condition and probable contribution on a per site basis.

The Corporation is implementing an Administrative Order on Consent entered into with the Michigan Department of Natural Resources and the Environmental Protection Agency regarding an investigation of the Kalamazoo River and two disposal areas which are contaminated with polychlorinated biphenyls. Data regarding the extent of contamination at the two disposal areas has been evaluated. The cost to remediate one of the disposal areas was estimated at $8 million and this site has been essentially closed. It is anticipated that the cost of remediation of the second disposal area will be at least equal to that amount,

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however, the Corporation is still negotiating a final closing agreement with the State of Michigan. Fort James is not a signatory to the Administrative Order on Consent.

A draft Remedial Investigation/ Feasibility Study ("RI/FS") for the Kalamazoo River was submitted to the State of Michigan on October 30, 2000 by the Corporation and other potentially responsible parties ("PRPs"), including Fort James Corporation. The PRPs' draft RI/FS evaluated five remedial options ranging from no action to total dredging of the river and off-site disposal of the dredged materials. The cost for these remedial options ranges from $0 to $2.5 billion. The PRPs' draft RI/FS recommends a remedy involving stabilization of over twenty miles of river bank and long term monitoring of the river bed. However, the State of Michigan has asked for additional possible remedies. The total cost for the PRPs' recommended remedy is approximately $73 million.

Fort James has been identified as a PRP for contamination of the Lower Fox River and Green Bay system in Wisconsin by hazardous substances. Various state and federal agencies and tribal entities are seeking both sediment restoration and natural resources damages. In February 1999, the Wisconsin Department of Natural Resources ("WDNR") released for public comment a draft remedial investigation/feasibility study of the Fox River. While the draft study did not advocate any specific restoration alternatives, it included estimated total costs ranging from zero for "no action" to approximately $720 million, depending on the alternative or combination of alternatives selected.

In June 2000, Fort James voluntarily entered into an agreement with the WDNR and the EPA for the restoration of one sediment area on the Fox River. The project began in August 2000 and was completed on December 15, 2000 at a cost of approximately $8 million.

In October 2000, the U.S. Fish and Wildlife Service ("FWS") released for public comment its Restoration and Compensation Determination Plan (the "Plan") for natural resources damages in connection with its Lower Fox River/Green Bay Natural Resource Damage Assessment. According to the Plan, claims for past damages and present and future losses allegedly resulting from contamination of the Fox River by hazardous substances range from $176 million to $333 million, depending on the sediment restoration alternative or combinations of alternatives selected. The actual costs of projects to settle natural resource damage claims could be significantly lower.

In November 2000, Fort James entered into a settlement with WDNR that resolves the State's natural resource damages claims against Fort James under CERCLA, the Federal Water Pollution Control Act, and state law**.** Under the agreement, Fort James has agreed to spend approximately $7 million. The agreement will be effective when entered by the federal court.

The final cleanup alternatives and the Corporation's share of the related costs, for both the Fox River and Kalamazoo River matters, are unknown at this time.

The Corporation and many other companies are defendants in suits brought in various courts around the nation by plaintiffs who allege that they have suffered personal injury as a result of exposure to asbestos-containing products. These suits allege a variety of lung and other diseases based on alleged exposure to products previously manufactured by the Corporation. In many cases, the plaintiffs are unable to demonstrate that they have suffered any compensable loss as a result of such exposure, or that any injuries they have incurred in fact resulted from exposure to the Corporation's products.

The Corporation is currently defending the claims of approximately 65,674 such plaintiffs as of March 31, 2001, and anticipates that additional claims will be filed against it over the next several years. The number of claims filed against the Corporation, and the average cost of resolving such claims, has increased somewhat over the last three years. The Corporation generally settles asbestos cases for amounts it considers reasonable given the facts and circumstances of each case. Substantially all of the amounts it has paid to date to defend and resolve these cases have been covered by product liability insurance. The Corporation has agreements with its insurers to utilize insurance in amounts which it believes are adequate to cover substantially all of the defense costs and liabilities for currently pending cases, as well as the reasonably

foreseeable defense costs and liabilities attributable to claims which may be filed against it over the next several years. The Corporation has additional insurance coverage which it believes will cover a substantial part of the defense costs and liabilities attributable to additional future claims for some period of years, depending on the number of claims filed each year in the future and the average cost of resolving each such claim. However, there can be no assurance that such coverage will be adequate to cover the costs of all future claims, or that the part of such defense costs and liabilities not covered by such insurance will not be material to the Corporation. The Corporation has established reserves with respect to pending cases for the liabilities and defense costs it believes are probable and reasonably estimable, and has also established a receivable for insurance to the extent that the realization of the claim is deemed probable.

On May 6, 1998, a lawsuit was filed in state court in Columbus, Ohio, against the Corporation and Georgia-Pacific Resins, Inc. (GPR), a wholly owned subsidiary of the Corporation. The lawsuit was filed by eight plaintiffs who seek to represent a class of individuals who at any time from 1985 to the present lived, worked, resided, owned, frequented or otherwise occupied property located within a three-mile radius of GPR's resins manufacturing operations in Columbus, Ohio. The lawsuit alleges that the individual plaintiffs and putative class members have suffered personal injuries and/or property damage because of (i) alleged "continuing and long-term releases and threats of releases of noxious fumes, odors and harmful chemicals, including hazardous substances" from GPR's operations and/or (ii) a September 10, 1997 explosion at the Columbus facility and alleged release of hazardous material resulting from that explosion. Virtually all activity in this case has been stayed pending a decision on a motion by plaintiffs for reconsideration of a case management order issued by the court. The Corporation has denied the material allegations of this lawsuit. While it is premature to evaluate the claims asserted in this lawsuit, the Corporation believes it has meritorious defenses. Prior to the filing of the lawsuit,