Rock-Tenn CO
Form 10-Q
April 30, 2007

Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
Form 10-Q

þ **Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**

For the quarterly period ended March 31, 2007

or

o **Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**

For the transition period from __________ to __________
Commission File Number 0-23340
Rock-Tenn Company
(Exact Name of Registrant as Specified in Its Charter)

Georgia	**62-0342590**
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)
504 Thrasher Street, Norcross, Georgia	**30071**
(Address of Principal Executive Offices)	(Zip Code)

Registrant s Telephone Number, Including Area Code: **(770) 448-2193**
N/A
(Former Name, Former Address and Former Fiscal Year, if Changed Since Last Report.)

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer or a non-accelerated filer (as defined in Rule 12b-2 of the Exchange Act).

Large accelerated filer o Accelerated filer þ Non-accelerated filer o

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

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date:

Class	Outstanding as of April 19, 2007
Class A Common Stock, $0.01 par value	40,076,222

ROCK-TENN COMPANY
INDEX

Table of Contents

PART I: FINANCIAL INFORMATION

Item 1. ***FINANCIAL STATEMENTS (UNAUDITED)***

ROCK-TENN COMPANY
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)
(In Millions, Except Per Share Data)

	Three Months Ended March 31,		Six Months Ended March 31,	
	2007	2006	2007	2006
Net sales	$ 585.7	$ 529.7	$ 1,119.6	$ 1,020.1
Cost of goods sold	473.3	440.5	909.6	871.3
Gross profit	112.4	89.2	210.0	148.8
Selling, general and administrative expenses	63.5	62.0	124.8	119.1
Restructuring and other costs, net	1.2	3.5	1.7	4.5
Operating profit	47.7	23.7	83.5	25.2
Interest expense	(12.3)	(13.9)	(25.3)	(27.8)
Interest and other income		0.6	0.2	0.6
Equity in income (loss) of unconsolidated entities	0.4	(0.2)	0.7	1.4
Minority interest in income of consolidated subsidiaries	(1.1)	(1.8)	(3.0)	(3.1)
Income (loss) before income taxes	34.7	8.4	56.1	(3.7)
Income tax expense	(13.0)	(3.2)	(19.3)	(0.1)
Net income (loss)	$ 21.7	$ 5.2	$ 36.8	$ (3.8)
Weighted average diluted shares outstanding	39.8	36.7	39.3	35.9
Basic earnings (loss) per share:				
Net income (loss)	$ 0.56	$ 0.15	$ 0.97	$ (0.10)
Diluted earnings (loss) per share:				
Net income (loss)	$ 0.55	$ 0.14	$ 0.94	$ (0.10)
Cash dividends paid per common share	$ 0.10	$ 0.09	$ 0.19	$ 0.18

See Accompanying Notes to Condensed Consolidated Financial Statements

Table of Contents

ROCK-TENN COMPANY
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)
(In Millions, Except Per Share Data)

	March 31, 2007	September 30, 2006
ASSETS		
Current Assets:		
Cash and cash equivalents	$ 11.6	$ 6.9
Accounts receivable (net of allowances of $5.2 and $5.2)	231.7	230.8
Inventories	220.6	218.9
Other current assets	34.8	25.0
Assets held for sale	2.3	4.0
Total current assets	501.0	485.6
Property, plant and equipment at cost:		
Land and buildings	267.0	266.0
Machinery and equipment	1,325.0	1,299.7
Transportation equipment	10.7	10.8
Leasehold improvements	6.1	6.2
	1,608.8	1,582.7
Less accumulated depreciation and amortization	(770.8)	(732.1)
Net property, plant and equipment	838.0	850.6
Goodwill	364.0	356.6
Intangibles, net	66.0	55.1
Investment in unconsolidated entities	26.9	21.6
Other assets	15.5	14.5
	$ 1,811.4	$ 1,784.0
LIABILITIES AND SHAREHOLDERS EQUITY		
Current liabilities:		
Current portion of debt	$ 125.8	$ 40.8
Accounts payable	129.7	141.8
Accrued compensation and benefits	62.3	65.7
Other current liabilities	51.7	57.7
Total current liabilities	369.5	306.0
Long-term debt due after one year	647.3	754.9
Hedge adjustments resulting from terminated fair value interest rate derivatives or swaps	9.5	10.4
Total long-term debt	656.8	765.3

Accrued pension and other long-term benefits	77.4	75.9
Deferred income taxes	108.1	99.8
Other long-term liabilities	9.7	9.6
Commitments and contingencies (Note 11)		
Minority interest	11.0	18.8
Shareholders equity:		
Preferred stock, $0.01 par value; 50,000,000 shares authorized; no shares outstanding		
Class A common stock, $0.01 par value; 175,000,000 shares authorized; 40,068,222 and 37,688,522 shares outstanding at March 31, 2007 and September 30, 2006, respectively	0.4	0.4
Capital in excess of par value	229.2	179.6
Retained earnings	368.7	341.2
Accumulated other comprehensive loss	(19.4)	(12.6)
Total shareholders equity	578.9	508.6
	$ 1,811.4	$ 1,784.0

See Accompanying Notes to Condensed Consolidated Financial Statements

Table of Contents

ROCK-TENN COMPANY
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)
(In Millions)

	Six Months Ended March 31, 2007	Six Months Ended March 31, 2006
Operating activities:		
Net income (loss)	$ 36.8	$ (3.8)
Items in income not affecting cash:		
Depreciation and amortization	51.5	51.7
Deferred income tax expense	8.7	7.3
Share-based compensation expense	3.6	1.5
Loss on disposal of plant, equipment and other, net	1.2	0.1
Minority interest in income of consolidated subsidiaries	3.0	3.1
Equity in income of unconsolidated entities	(0.7)	(1.4)
Proceeds from (payment on) termination of cash flow interest rate hedges	(0.2)	9.9
Pension funding (more) less than expense	1.8	(0.3)
Impairment adjustments and other non-cash items	0.1	1.7
Change in operating assets and liabilities, net of acquisitions:		
Accounts receivable	(1.8)	(5.6)
Inventories	(2.6)	(4.9)
Other assets	(3.5)	(7.2)
Accounts payable	(11.9)	26.0
Income taxes payable	(9.7)	(11.0)
Accrued liabilities	(7.1)	(4.3)
Net cash provided by operating activities	69.2	62.8
Investing activities:		
Capital expenditures	(40.8)	(27.1)
Cash paid for purchase of businesses, net of cash received	(32.0)	(7.8)
Investment in unconsolidated entity	(8.6)	
Cash contributed to unconsolidated entity	(0.1)	
Return of capital from unconsolidated entity	4.1	
Proceeds from sale of property, plant and equipment	2.3	0.8
Proceeds from property, plant and equipment insurance settlement	0.4	
Net cash used for investing activities	(74.7)	(34.1)
Financing activities:		
Additions to revolving credit facilities	32.0	60.5
Repayments of revolving credit facilities	(60.2)	(126.4)
Additions to debt	21.9	31.4
Repayments of debt	(14.4)	(13.4)
Debt issuance costs		(0.3)
Issuances of common stock	30.0	2.9
Excess tax benefits from share-based compensation	14.2	0.1
Capital contributed to consolidated subsidiary from minority interest		2.1
Advances from (repayments to) unconsolidated entity	(5.0)	5.6

Cash dividends paid to shareholders	(7.4)	(6.6)
Cash distributions to minority interest	(1.3)	(2.9)
Net cash provided by (used for) financing activities	9.8	(47.0)
Effect of exchange rate changes on cash and cash equivalents	0.4	(0.4)
Increase (decrease) in cash and cash equivalents	4.7	(18.7)
Cash and cash equivalents at beginning of period	6.9	26.8
Cash and cash equivalents at end of period	$ 11.6	$ 8.1
Supplemental disclosure of cash flow information:		
Cash paid during the period for:		
Income taxes, net of refunds	$ 6.1	$ 4.0
Interest, net of amounts capitalized	28.2	29.2

See Accompanying Notes to Condensed Consolidated Financial Statements

3

Table of Contents

ROCK-TENN COMPANY
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
For the Three and Six Month Periods Ended March 31, 2007
(Unaudited)

Unless the context otherwise requires, ***we*** *,* ***us*** *,* ***our*** *,* ***Rock-Tenn*** *and* ***the Company*** *refer to the business of Rock-Tenn Company and its consolidated subsidiaries, including RTS Packaging, LLC (* ***RTS*** *) and GSD Packaging, LLC (* ***GSD*** *). We own 65% of RTS and conduct our interior packaging products business through RTS. At December 31, 2006 we owned 60% of GSD and conducted some of our folding carton operations through GSD. In January 2007, we acquired the outstanding 40% of GSD. These terms do not include Seven Hills Paperboard, LLC (* ***Seven Hills*** *) or Quality Packaging Specialists International, LLC (* ***QPSI*** *). We own 49% of Seven Hills, a manufacturer of gypsum paperboard liner, and 23.96% of QPSI, a business providing merchandising displays, contract packing, logistics and distribution solutions, neither of which we consolidate. All references in the accompanying condensed consolidated financial statements and this Quarterly Report on Form 10-Q to data regarding sales price per ton and fiber, energy, chemical and freight costs with respect to our recycled paperboard mills excludes that data with respect to our Aurora, Illinois, recycled paperboard mill, which sells only converted products and which would not be material. All other references herein to operating data with respect to our recycled paperboard mills, including tons data and capacity utilization rates, includes operating data from our Aurora mill.*

Note 1. Interim Financial Statements

Our independent registered public accounting firm has not audited our accompanying condensed consolidated financial statements. We derived the condensed consolidated balance sheet at September 30, 2006 from the audited consolidated financial statements. In the opinion of our management, the condensed consolidated financial statements reflect all adjustments, which are of a normal recurring nature, necessary for a fair presentation of our results of operations for the three and six months ended March 31, 2007 and 2006, our financial position at March 31, 2007 and September 30, 2006, and our cash flows for the six months ended March 31, 2007 and 2006.

We have condensed or omitted certain notes and other information from the interim financial statements presented in this Quarterly Report on Form 10-Q. Therefore, these condensed consolidated financial statements should be read in conjunction with our Annual Report on Form 10-K for the fiscal year ended September 30, 2006 (the **Fiscal 2006 Form 10-K**).

The results for the three and six months ended March 31, 2007 are not necessarily indicative of results that may be expected for the full year.

We have made certain reclassifications to prior year amounts to conform such amounts to the current year presentation.

Note 2. New Accounting Standards

Recently Issued Standards

In February 2007, the Financial Accounting Standards Board (**FASB**) issued Statement of Financial Accounting Standards (**SFAS**) No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities Including an Amendment of FASB Statement No. 115* (**SFAS 159**). SFAS No. 159 permits entities to choose to measure many financial instruments and certain other items at fair value. This provides entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without being required to apply complex hedge accounting provisions. The provisions of SFAS No. 159 are effective as of the beginning of fiscal years that start after November 15, 2007 (October 1, 2008 for us). Management is currently evaluating the impact that SFAS No. 159 will have on our financial position and results of operations upon adoption.

Table of Contents

Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

In July 2006, the FASB released FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes an Interpretation of FASB Statement 109* (**FIN 48**). FIN 48 prescribes a comprehensive model for how a company should recognize, measure, present, and disclose in its financial statements uncertain tax positions that the company has taken or expects to take on a tax return (including a decision whether to file or not to file a return in a particular jurisdiction). Under FIN 48, the consolidated financial statements will reflect expected future tax consequences of such positions presuming the taxing authorities full knowledge of the position and all relevant facts, but without considering time values. FIN 48 is likely to cause greater volatility in earnings as more items are recognized discretely within income tax expense. FIN 48 also revises disclosure requirements and introduces a prescriptive, annual, tabular roll-forward of the unrecognized tax benefits. FIN 48 is effective as of the beginning of fiscal years that start after December 15, 2006 (October 1, 2007 for us). Management is currently evaluating the impact that FIN 48 will have on our financial position and results of operations upon adoption.

In September 2006, the FASB released Statement of Financial Accounting Standards No. 157, *Fair Value Measurements* (**SFAS 157**). SFAS 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles (**GAAP**), and expands disclosures about fair value measurements. SFAS 157 emphasizes that fair value is a market-based measurement, not an entity-specific measurement. Therefore, a fair value measurement would be determined based on the assumptions that market participants would use in pricing the asset or liability. SFAS 157 is effective for fiscal years beginning after November 15, 2007 (October 1, 2008 for us). Management is presently evaluating the impact, if any, upon adoption.

In September 2006, the FASB released SFAS No. 158, *Employers Accounting for Defined Benefit Pension and Other Postretirement Plans, an amendment of FASB Statements No. 87, 88, 106, and 132(R)* (**SFAS 158**). SFAS 158 requires companies to:

Recognize the funded status of a benefit plan in its statement of financial position.

Recognize as a component of other comprehensive income, net of tax, the gains or losses and prior service costs or credits that arise during the period but are not recognized as components of net periodic benefit cost.

Measure defined benefit plan assets and obligations as of the date of the employer s fiscal year-end statement of financial position (with limited exceptions).

Provide additional disclosure in the Consolidated Financial Statements.

SFAS 158 does not impact the determination of net periodic benefit cost recognized in the income statement. We must adopt SFAS 158 as of the end of our fiscal year ending September 30, 2007. Had we adopted SFAS 158 at September 30, 2006, the impact would have been as follows: total assets would have been approximately $3 million lower, total liabilities would have been approximately $9 million higher and shareholders equity would have been approximately $12 million lower. Because our net pension liabilities are dependent upon future events and circumstances, the impact at the time of adoption of SFAS 158 may differ from these amounts.

Note 3. Comprehensive Income (Loss)

The following are the components of comprehensive income (loss) (in millions):

	Three Months Ended March 31,		Six Months Ended March 31,	
	2007	2006	2007	2006
Net income (loss)	$ 21.7	$ 5.2	$ 36.8	$ (3.8)
Foreign currency translation adjustments	0.9	(0.7)	(3.8)	(1.2)
Reclassification of previously terminated hedges to earnings, net of tax	(0.6)	(0.2)	(1.3)	(0.2)
Net unrealized gain on derivative instruments, net of tax	(1.8)	1.6	(1.7)	3.2

Comprehensive income (loss)	$ 20.2	$ 5.9	$ 30.0	$ (2.0)

The change in other comprehensive income (loss) due to foreign currency translation was primarily due to the change in the Canadian/U.S. dollar exchange rates.

Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

Note 4. Earnings (Loss) per Share

The following table sets forth the computation of basic and diluted earnings (loss) per share (in millions, except per share data):

	Three Months Ended March 31,		Six Months Ended March 31,	
	2007	2006	2007	2006
Numerator:				
Net income (loss)	$ 21.7	$ 5.2	$ 36.8	$ (3.8)
Denominator:				
Denominator for basic earnings (loss) per share weighted average shares	38.7	35.9	38.0	35.9
Effect of dilutive stock options and restricted stock awards	1.1	0.8	1.3	
Denominator for diluted earnings (loss) per share weighted average shares and assumed conversions	39.8	36.7	39.3	35.9
Basic earnings (loss) per share:				
Net income (loss) per share basic	$ 0.56	$ 0.15	$ 0.97	$ (0.10)
Diluted earnings (loss) per share:				
Net income (loss) per share diluted	$ 0.55	$ 0.14	$ 0.94	$ (0.10)

All outstanding options to purchase common shares were dilutive at March 31, 2007 and were included in the effect of dilutive securities. Due to the net loss for the six months ended March 31, 2006, the assumed net exercise of stock options and restricted stock awards was excluded, as the effect would have been anti-dilutive. Options and restricted stock awards for 3.9 million and 0.5 million shares of common stock, respectively, were excluded from the six months ended March 31, 2006 calculation because their effect was anti-dilutive. If we had not had a loss, approximately 0.7 million shares of dilutive stock options and restricted stock awards would have been included in the denominator for the six months ended March 31, 2006. During the six months ended March 31, 2007 and 2006, 2.4 million and 0.3 million shares of common stock, respectively, were issued primarily due to the exercise of stock options.

The table below summarizes the changes in all stock options during the six months ended March 31, 2007:

	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value (in millions)
Outstanding at September 30, 2006	3,211,369	$ 13.83		
Granted				
Exercised	(2,211,301)	13.72		
Expired	(10,600)	18.66		
Forfeited				
Outstanding at March 31, 2007	989,468	$ 14.01	6.3 years	$ 19.0

Exercisable at March 31, 2007	927,471	$	13.88	6.1 years	$	17.9

The aggregate intrinsic value of options exercised during the three months ended March 31, 2007 and 2006 was $19.7 million and $0.1 million, respectively. The aggregate intrinsic value of options exercised during the six months ended March 31, 2007 and 2006 was $33.0 million and $0.2 million, respectively.

Table of Contents

Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

Note 5. Acquisitions

Folding Cartons

On January 24, 2007, we acquired for $32.0 million the remaining 40% minority interest in GSD, giving us sole ownership of the company. We acquired our initial 60% interest in GSD in connection with the Gulf States Acquisition (as defined below) in June 2005. GSD makes paperboard-based food containers serving a very broad customer base and is a consumer of board from our bleached paperboard mill. The acquisition included a preliminary allocation of approximately $13.9 million to intangibles, primarily for customer relationships and approximately $8.3 million to goodwill. We expect the goodwill to be deductible for income tax purposes. The allocation of the purchase price is subject to the finalization of appraisals and the pro forma impact of the acquisition is not material to our financial results.

Interior Packaging

On February 27, 2006, our RTS subsidiary completed the acquisition of the partition business of Caraustar Industries, Inc. for an aggregate purchase price of $6.1 million. This acquisition by RTS was funded by capital contributions to RTS by us and our minority interest partner in proportion to our respective investments in RTS and was accounted for as a purchase of a business. We have included these operations in our condensed consolidated financial statements since that date in our Packaging Products segment. RTS acquired this business, which manufactures high quality die cut partitions, in order to gain entrance into the specialty partition market. The acquisition included $2.4 million of goodwill. We expect the goodwill to be deductible for income tax purposes. The pro forma impact of the acquisition is not material to our financial results.

Table of Contents

Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

Note 6. Restructuring and Other Costs, Net

Summary of Restructuring and Other Initiatives

We recorded pre-tax restructuring and other costs, net, of $1.2 million and $3.5 million for the three months ended March 31, 2007 and 2006, respectively, and recorded pre-tax restructuring and other costs, net, of $1.7 million and $4.5 million for the six months ended March 31, 2007 and 2006, respectively. These amounts are not comparable since the timing and scope of the individual actions associated with a restructuring can vary. We discuss these charges in more detail below.

The following table represents a summary of restructuring and other charges, net, related to our active restructuring initiatives that we incurred during the three and six months ended March 31, 2007 and 2006, respectively, cumulatively since we announced each initiative, and the total we expect to incur (in millions):

Initiative and Segment	Period	Net Property, Plant and Equipment[(a)]	Severance and Other Employee Related Costs	Equipment and Inventory Relocation	Facility Carrying Costs	Other	Total
Stone Mountain,	Current Qtr.	$ 0.4	$ 0.9	$	$	$ 0.2	$ 1.5
Packaging	Fiscal 2007	0.4	0.9			0.2	1.5
Products[(b)]	Prior Year Qtr.						
	Fiscal 2006						
	Cumulative	0.4	0.9				