

GLATFELTER P H CO  
Form 10-Q  
November 09, 2007

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549  
FORM 10-Q

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

or

**TRANSITION REPORT PURSUANT TO SECTION 13 or 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE TRANSITION PERIOD**

from \_\_\_\_\_ to \_\_\_\_\_

For the quarterly period ended **September 30, 2007**

Commission file number **1-3560**

**P. H. Glatfelter Company**

(Exact name of registrant as specified in its charter)

**Pennsylvania**

(State or other jurisdiction of  
incorporation or organization)

**23-0628360**

(IRS Employer Identification No.)

**96 South George Street, Suite 500**

**York, Pennsylvania 17401**

(Address of principal executive offices)

**(717) 225-4711**

(Registrant's telephone number, including area code)

**N/A**

(Former name or former address, 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 at least the past 90 days. Yes  No .

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act.  
 Large Accelerated  Accelerated  Non-Accelerated.

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

As of October 31, 2007, P. H. Glatfelter Company had 45,112,001 shares of common stock outstanding.

**P. H. GLATFELTER COMPANY**  
**REPORT ON FORM 10-Q**  
**for the QUARTERLY PERIOD ENDED**  
**September 30, 2007**  
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**PART I****Item 1 Financial Statements****CONDENSED CONSOLIDATED STATEMENTS OF INCOME**

**P. H. GLATFELTER COMPANY**  
**CONDENSED CONSOLIDATED STATEMENTS OF INCOME**  
(unaudited)

	<b>Three Months Ended</b>		<b>Nine Months Ended</b>	
	<b>September 30</b>		<b>September 30</b>	
<i>In thousands, except per share</i>	<b>2007</b>	2006	<b>2007</b>	2006
Net sales	<b>\$ 291,859</b>	\$ 277,489	<b>\$ 860,939</b>	\$ 717,815
Energy sales net	<b>2,491</b>	2,706	<b>7,129</b>	8,010
Total revenues	<b>294,350</b>	280,195	<b>868,068</b>	725,825
Costs of products sold	<b>247,470</b>	242,292	<b>755,679</b>	661,924
Gross profit	<b>46,880</b>	37,903	<b>112,389</b>	63,901
Selling, general and administrative expenses	<b>42,197</b>	24,590	<b>94,700</b>	66,327
Shutdown and restructuring charges		2,222	<b>162</b>	28,177
Gains on dispositions of plant, equipment and timberlands, net	<b>(2,301)</b>	(923)	<b>(11,188)</b>	(2,008)
Gains from insurance recoveries				(205)
Operating income (loss)	<b>6,984</b>	12,014	<b>28,715</b>	(28,390)
Non-operating income (expense)				
Interest expense	<b>(7,569)</b>	(7,012)	<b>(22,330)</b>	(17,575)
Interest income	<b>979</b>	558	<b>2,568</b>	2,350
Other net	<b>113</b>	704	<b>380</b>	(840)
Total other income (expense)	<b>(6,477)</b>	(5,750)	<b>(19,382)</b>	(16,065)
Income (loss) before income taxes	<b>507</b>	6,264	<b>9,333</b>	(44,455)
Income tax provision (benefit)	<b>(7,305)</b>	896	<b>(3,730)</b>	(17,238)
Net income (loss)	<b>\$ 7,812</b>	\$ 5,368	<b>\$ 13,063</b>	\$ (27,217)
<b>Earnings (loss) per share</b>				
Basic and diluted	<b>\$ 0.17</b>	\$ 0.12	<b>\$ 0.29</b>	\$ (0.61)
<b>Cash dividends declared per common share</b>	<b>\$ 0.09</b>	\$ 0.09	<b>\$ 0.27</b>	\$ 0.27
<b>Weighted average shares outstanding</b>				
Basic	<b>45,084</b>	44,749	<b>45,004</b>	44,512
Diluted	<b>45,364</b>	45,247	<b>45,365</b>	44,512

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

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**CONDENSED CONSOLIDATED BALANCE SHEETS**

**P. H. GLATFELTER COMPANY**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**  
(unaudited)

<i>In thousands</i>	<b>September 30 2007</b>	December 31 2006
<b>Assets</b>		
<b>Current assets</b>		
Cash and cash equivalents	\$ 17,820	\$ 21,985
Accounts receivable net	136,550	128,255
Inventories	185,508	192,281
Prepaid expenses and other current assets	31,982	32,517
Total current assets	<b>371,860</b>	375,038
<b>Plant, equipment and timberlands net</b>	<b>519,416</b>	528,867
<b>Other assets</b>	<b>329,057</b>	321,738
Total assets	<b>\$ 1,220,333</b>	\$ 1,225,643
<b>Liabilities and Shareholders Equity</b>		
<b>Current liabilities</b>		
Current portion of long-term debt	\$ 49,532	\$ 19,500
Short-term debt	1,155	2,818
Accounts payable	62,269	70,966
Dividends payable	4,060	4,035
Environmental liabilities	8,685	5,489
Other current liabilities	92,207	90,482
Total current liabilities	<b>217,908</b>	193,290
<b>Long-term debt</b>	<b>302,565</b>	375,295
<b>Deferred income taxes</b>	<b>165,389</b>	182,659
<b>Other long-term liabilities</b>	<b>123,233</b>	86,031
Total liabilities	<b>809,095</b>	837,275
<b>Commitments and contingencies</b>		
<b>Shareholders equity</b>		
Common stock	544	544

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Capital in excess of par value	<b>44,054</b>	42,288
Retained earnings	<b>517,263</b>	519,489
Accumulated other comprehensive loss	<b>(13,196)</b>	(32,337)
	<b>548,665</b>	529,984
Less cost of common stock in treasury	<b>(137,427)</b>	(141,616)
Total shareholders' equity	<b>411,238</b>	388,368
Total liabilities and shareholders' equity	<b>\$ 1,220,333</b>	\$ 1,225,643

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

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**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**P. H. GLATFELTER COMPANY**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(unaudited)

<i>In thousands</i>	<b>Nine Months Ended September 30</b>	
	<b>2007</b>	<b>2006</b>
<b>Operating activities</b>		
Net income (loss)	\$ 13,063	\$ (27,217)
Adjustments to reconcile to net cash provided (used) by operations:		
Depreciation and depletion	42,293	37,122
Provision for environmental matters	26,000	
Pension income	(9,646)	(12,644)
Restructuring charges	162	33,328
Deferred income tax provision	(11,843)	(10,387)
(Gains) losses on dispositions of plant, equipment and timberlands, net	(11,188)	(2,008)
Stock-based compensation	2,975	1,733
Change in operating assets and liabilities		
Accounts receivable	(5,320)	(26,160)
Inventories	10,168	(968)
Other assets and prepaid expenses	819	(6,147)
Accounts payable	(9,280)	(9,980)
Other current liabilities	12,297	(23,076)
Other	(2,737)	64
Net cash provided (used) by operating activities	<b>57,763</b>	(46,340)
<b>Investing activities</b>		
Purchases of plant, equipment and timberlands	(19,289)	(35,225)
Proceeds from disposals of plant, equipment and timberlands	12,099	2,975
Acquisition of Lydney mill and Chillicothe		(158,148)
Net cash used by investing activities	<b>(7,190)</b>	(190,398)
<b>Financing activities</b>		
Net (repayment of) proceeds from revolving credit facility	(20,656)	55,819
Principal repayment on term loan	(23,000)	(560)
Proceeds from \$100 million term loan facility, net of issuance costs		98,829
Net proceeds from \$200 million, 7 <sup>1</sup> / <sub>8</sub> % note offering		196,440
Repayment of \$150 million 6 <sup>7</sup> / <sub>8</sub> % notes, including early redemption premium		(152,675)
Net repayment of other short-term debt	(1,767)	
Payment of dividends	(12,253)	(11,993)
Proceeds from stock options exercised	1,384	7,322
Excess tax benefit of stock options exercised	93	768
Net cash (used) provided by financing activities	<b>(56,199)</b>	193,950



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Effect of exchange rate changes on cash	<b>1,461</b>	(773)
Net decrease in cash and cash equivalents	<b>(4,165)</b>	(43,561)
Cash and cash equivalents at the beginning of period	<b>21,985</b>	57,442
Cash and cash equivalents at the end of period	<b>\$ 17,820</b>	\$ 13,881
 <b>Supplemental cash flow information</b>		
Cash paid for interest	<b>\$ 18,555</b>	\$ 14,619
Cash paid (received) for income taxes	<b>(900)</b>	17,436

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

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**P. H. GLATFELTER COMPANY AND SUBSIDIARIES**  
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

unaudited

**1. ORGANIZATION**

P. H. Glatfelter Company and subsidiaries ( Glatfelter ) is a manufacturer of specialty papers and engineered products. Headquartered in York, Pennsylvania, our manufacturing facilities are located in Spring Grove, Pennsylvania; Chillicothe and Fremont, Ohio; Lydney, Gloucestershire, the United Kingdom; Gernsbach, Germany; Scaër, France and the Philippines. Our products are marketed throughout the United States and in over 80 other countries, either through wholesale paper merchants, brokers and agents, or directly to customers.

**2. ACCOUNTING POLICIES**

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

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

**Reclassifications** Certain reclassifications have been made to the prior year's balance sheet, specifically between accounts payable and other current liabilities, to conform to those classifications used in the current year. Such reclassifications had no impact on reported earnings, financial position, or cash flows for either period.

**3. RECENT PRONOUNCEMENTS**

Effective January 1, 2007, we adopted the provisions of FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109 ( FIN 48 ). The Interpretation prescribes a recognition threshold and a measurement attribute for the financial statement recognition and measurement of tax positions taken or expected to be taken in a tax return. For those benefits to be recognized, a tax position must be more-likely-than-not to be sustained upon examination by taxing authorities. The amount recognized is measured as the largest amount of benefit that is greater than 50 percent likely of being realized upon ultimate settlement. The cumulative effect adjustment of \$3.0 million was recognized as an adjustment to retained earnings.

The following table provides a breakdown of the incremental effect of applying FIN 48 on individual line items in the consolidated balance sheet as of January 1, 2007:

<i>In thousands</i>	Before FIN 48	Effect of FIN 48	After adoption of FIN 48
Prepaid expenses and other current assets	\$ 32,517	\$ 193	\$ 32,710
Other current liabilities	90,482	(7,214)	83,268
Other long-term liabilities	86,031	21,690	107,721
Deferred income taxes	182,659	(11,309)	171,350
Retained earnings	519,489	(2,974)	516,515

In September 2006, SFAS No. 157, Fair Value Measurements was issued. SFAS No. 157, which defines fair value, establishes a framework for measurement and requires expanded disclosures about the fair value measurements, is effective for us beginning January 1, 2008. We do not expect the adoption of SFAS No. 157 to have a material impact on our consolidated financial position or results of operations.

**4. ACQUISITIONS**

**Lydney** On March 8, 2006, we entered into a definitive agreement to acquire, through Glatfelter-UK Limited ( GLT-UK ), a wholly-owned subsidiary, certain assets and liabilities of J R Crompton Limited ( Crompton ), a global supplier of wet laid non-woven products based in Manchester, United Kingdom. On February 7, 2006, Crompton was placed into Administration, the U.K. equivalent of bankruptcy.

Effective March 13, 2006, we completed our purchase of Crompton s Lydney mill and related inventory, located in Gloucestershire, UK for £37.5 million (US \$65.0 million) in cash in addition to \$4.2 million of transaction costs. The Lydney facility employed about 240 people and, produced a broad portfolio of wet laid non-woven products, including tea and coffee filter papers, clean room wipes, lens tissue, dye filter paper, double-sided adhesive tape substrates and

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battery grid pasting tissue, and had 2005 revenues of approximately £43 million (US \$75 million). The purchase price was financed with existing cash balances and borrowings under our credit facility.

The following table summarizes the allocation of the purchase price to assets acquired and liabilities assumed:

*In thousands*

**Assets acquired:**

Inventory	\$ 8,389
Property and equipment	56,885
Intangibles and other assets	9,325
	74,599
Less acquisition related liabilities	(5,374)
Total	\$ 69,225

Although we do not expect future adjustments to occur, any such adjustments required to be made to the purchase price allocation will be reflected in our results of operations in the applicable period in which such adjustment occurs. The amounts set forth above ascribed to intangible and other assets primarily consist of technology and trademarks.

**Chillicothe** On April 3, 2006, we completed our acquisition of Chillicothe, the carbonless business operations of NewPage Corporation, for \$83.3 million in cash, in addition to approximately \$5.9 million of transaction and other related costs. The Chillicothe assets consist of a paper making facility in Chillicothe, Ohio with annual production capacity approximating 400,000 tons-per-year and coating operations based in Fremont, Ohio with annual revenue of approximately \$440 million. The Chillicothe acquisition was financed with borrowings under our credit facility.

The following table summarizes the allocation of the purchase price to assets acquired and liabilities assumed:

*In thousands*

**Assets acquired:**

Accounts receivable	\$ 43,618
Inventory	91,580
Property and equipment	1,959
Prepaid pension and other assets	11,416
Intangibles customer relationships	6,074
	154,647
Less acquisition related liabilities including accounts payable and accrued expenses	(65,430)
Total	\$ 89,217

Although we do not expect future adjustments to occur, any such adjustments required to be made to the purchase price allocation will be reflected in our results of operations in the applicable period in which such adjustment occurs.

**Pro-Forma Financial Information** The information necessary to provide certain pro forma financial data for the Chillicothe acquisition relative to net income and earnings per share is not readily available due to the nature of the accounting and reporting structure of the acquired operation prior to the acquisition date. Pro forma consolidated net sales for the nine months ended September 30, 2006 was \$823.7 million assuming the acquisition occurred at the beginning of the respective period. This unaudited pro forma financial information is not necessarily indicative of what the operating results would have been had the acquisition been completed at the beginning of the respective period nor is it indicative of future results.

**5. NEENAH FACILITY SHUTDOWN**

In connection with our agreement to acquire the Chillicothe operations, we committed to a plan to permanently close our Neenah, WI facility. Production at this facility ceased effective June 30, 2006 and certain products previously manufactured at the Neenah facility were transferred to Chillicothe.

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During the first nine months of 2007, we increased our reserve for costs associated with the shutdown by \$0.3 million and made payments totaling \$1.6 million; thus, the remaining reserve balance was \$1.5 million at September 30, 2007.

The results of operations in the first nine months of 2006 include the following pre-tax charges related to the Neenah shutdown:

<i>In thousands</i>	Beg. balance	Amount Accrued	Less non- cash- charges and cash payments	Balance Sept. 30, 2006
<b>Non-cash charges</b>				
Accelerated depreciation	\$	\$22,457	\$(22,457)	\$
Inventory write-down		3,196	(3,196)	
Pension curtailments and other retirement benefit charges		7,675	(7,675)	
Total non cash charges		33,328	(33,328)	
<b>Cash charges</b>				
Severance and benefit continuation		7,219	(3,432)	3,787
Contract termination costs		11,367	(11,367)	
Other		1,795	(645)	1,150
Total cash charges		20,381	(15,444)	4,937
Total	\$	\$53,709	\$(48,772)	\$4,937

The Neenah shutdown resulted in the elimination of approximately 200 positions that had been supporting our Specialty Papers business unit. Approximately \$25.7 million of the Neenah shutdown related charges are recorded as part of costs of products sold in the accompanying statements of income. The amounts accrued for severance and benefit continuation are recorded as other current liabilities in the accompanying consolidated balance sheets.

As part of the Neenah shutdown, we terminated our long-term steam supply contract, as provided for within the contract, resulting in termination fee of approximately \$11.4 million as of the end of the second quarter 2006.

#### **6. GAIN ON DISPOSITIONS OF PLANT, EQUIPMENT AND TIMBERLANDS**

During the first nine months of 2007 and 2006, gains on dispositions of plant, equipment and timberlands totaled \$11.2 million and \$2.0 million, respectively. Such gains are primarily from the completion of sales of timberlands which are summarized by the following table:

<i>Dollars in thousands</i>	Acres	Proceeds	Gain
2007	<b>4,674</b>	<b>\$11,649</b>	<b>\$11,223</b>
2006	465	1,573	1,503

In accordance with terms of our credit facility, we are required to use the after-tax proceeds from timberland sales to reduce amounts outstanding under our term loan.

#### **7. EARNINGS PER SHARE**

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

<i>In thousands, except per share</i>	<b>Three Months Ended September 30</b>	
	<b>2007</b>	<b>2006</b>
Net (loss) income	<b>\$ 7,812</b>	\$ 5,368
Weighted average common shares outstanding used in basic EPS	<b>45,084</b>	44,749
Common shares issuable upon exercise of dilutive stock options, restricted stock awards and performance awards	<b>280</b>	498
Weighted average common shares outstanding and common share equivalents used in diluted EPS	<b>45,364</b>	45,247
Potential common shares excluded due to anti-dilutive nature	<b>461</b>	399
Earnings (loss) per share Basic and diluted	<b>\$ 0.17</b>	\$ 0.12
<i>In thousands, except per share</i>	<b>Nine Months Ended September 30</b>	
	<b>2007</b>	<b>2006</b>
Net (loss) income	<b>\$13,063</b>	\$(27,217)
Weighted average common shares outstanding used in basic EPS	<b>45,004</b>	44,512
Common shares issuable upon exercise of dilutive stock options, restricted stock awards and performance awards	<b>361</b>	
Weighted average common shares outstanding and common share equivalents used in diluted EPS	<b>45,365</b>	44,512
Potential common shares excluded due to anti-dilutive nature	<b>458</b>	900
Earnings (loss) per share Basic and diluted	<b>\$ 0.29</b>	\$ (0.61)

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## 8. INCOME TAXES

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

Income taxes for the third quarter and first nine months of 2007 include \$5.3 million of tax benefit adjustments related to the revaluation of deferred tax assets and liabilities due to tax legislation enacted in July 2007 by Germany that reduced the corporate income tax rate.

Effective January 1, 2007, we adopted FIN 48. Subsequent to the adoption of this standard, we had \$21.5 million of gross unrecognized tax benefits. If recognized, approximately \$17.8 million would be recorded as a component of income tax expense, thereby affecting our effective tax rate. There have been no significant changes to these amounts during 2007 although we have resolved certain tax matters and closed certain open years.

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

Jurisdiction	Open Tax Year			
	Examination in progress		Examination not yet initiated	
United States				
Federal		N/A	2004	2006
State		2004	2002	2006
Germany (1)		N/A	2003	2006
France	2003	2005		2006
United Kingdom		N/A		2006
Philippines	2004	2006		N/A

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

The amount of income taxes we pay is subject to ongoing audits by federal, state and foreign tax authorities, which often result in proposed assessments. Management performs a comprehensive review of its global tax positions on a quarterly basis and accrues amounts for uncertain tax positions. Based on these reviews and the result of discussions and resolutions of matters with certain tax authorities and the closure of tax years subject to tax audit, reserves are adjusted as necessary. However, future results may include favorable or unfavorable adjustments to our estimated tax liabilities in the period the assessments are determined or resolved or as such statutes are closed. While it is possible that the amounts of unrecognized benefit with respect to uncertain tax positions could change significantly within the next twelve months, such adjustments, if any, are not expected to have a material effect on our consolidated financial position.

We recognize interest and penalties related to uncertain tax positions as income tax expense. Interest and penalty expense, net, totaled \$0.5 million and \$0.2 million for the first nine months of 2007 and the third quarter of 2007, respectively. Accrued interest and penalties were \$0.7 million and \$1.2 million as of January 1, 2007 and September 30, 2007, respectively.

## 9. STOCK-BASED COMPENSATION



During the first nine months of 2007, we issued, net of forfeitures, 217,100 Stock Only Stock Appreciation Rights ( SOSAR ) to members of executive management with a grant date strike price of \$15.94 per share. Under terms of the SOSAR, the recipients received the right to receive a payment in the form of shares of common stock equal to the difference if any, in the fair market value of one share of common stock at the time of exercising the SOSAR and the strike price. The SOSARs, which vest ratably over a three year period, had a grant date fair value, estimated using the Black-Scholes valuation model, of \$5.00 per right, and an aggregate value of \$1.1 million. In addition, 122,623 Restricted Stock Units ( RSU ) were issued in 2007 with a weighted-average grant date fair value of \$15.26 per unit and an aggregate value of \$1.9 million. The RSUs vest over a period ranging from three years to five years.

During the first nine months of 2007 and 2006, we recognized stock-based compensation expense totaling \$3.0 million and \$1.7 million, respectively.

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**10. RETIREMENT PLANS AND OTHER POST-RETIREMENT BENEFITS**

The following table provides information with respect to the net periodic costs of our pension and post retirement medical benefit plans.

<i>In thousands</i>	<b>Three Months Ended September 30</b>	
	<b>2007</b>	<b>2006</b>
<b>Pension Benefits</b>		
Service cost	\$ 2,392	\$ 1,762
Interest cost	5,452	5,698
Expected return on plan assets	(11,872)	(12,717)
Amortization of prior service cost	600	465
Recognized actuarial (gain)/loss	203	114
Net periodic benefit income	\$ (3,225)	\$ (4,678)
<b>Other Benefits</b>		
Service cost	\$ 506	\$ 449
Interest cost	759	780
Expected return on plan assets	(223)	
Amortization of prior service cost	(259)	(167)
Amortization of unrecognized loss	262	329
Net periodic benefit cost	\$ 1,045	\$ 1,391
	<b>Nine Months Ended September 30</b>	
<i>In thousands</i>	<b>2007</b>	<b>2006</b>
<b>Pension Benefits</b>		
Service cost	\$ 7,176	\$ 4,441
Interest cost	16,370	15,345
Expected return on plan assets	(35,600)	(34,483)
Amortization of prior service cost	1,799	1,381
Recognized actuarial (gain) loss	609	672
	(9,646)	(12,644)
Curtailment charge		4,403
Net periodic benefit income	\$ (9,646)	\$ (8,241)
<b>Other Benefits</b>		
Service cost	\$ 1,520	\$ 1,203
Interest cost	2,275	2,214
Expected return on assets	(669)	

Amortization of prior service cost	(776)	(542)
Amortization of unrecognized loss	786	977
	<b>3,136</b>	3,852
Special termination charge		3,273
Net periodic benefit cost	<b>\$ 3,136</b>	\$ 7,125

As discussed in Note 5, in the first quarter of 2006, we recorded special termination charges in connection with the curtailment of pension benefits and termination of certain post retirement benefits related to the Neenah facility shutdown.

During the fourth quarter of 2006, we transferred \$12.2 million from our qualified pension plan assets to a post-retirement sub-account pursuant to Section 420 of the Internal Revenue Code. Such amounts are to be used to satisfy certain post-retirement health care benefits.

## 11. COMPREHENSIVE INCOME

The following table sets forth comprehensive income and its components:

<i>In thousands</i>	<b>Three Months Ended September 30</b>	
	<b>2007</b>	2006
Net income (loss)	<b>\$ 7,812</b>	\$5,368
Foreign currency translation adjustment	<b>11,207</b>	856
Additional pension liability amortization, net of tax	<b>528</b>	
Comprehensive income (loss)	<b>\$19,547</b>	\$6,224

<i>In thousands</i>	<b>Nine Months Ended September 30</b>	
	<b>2007</b>	2006
Net income (loss)	<b>\$13,063</b>	\$(27,217)
Foreign currency translation adjustment	<b>17,623</b>	4,150
Additional pension liability amortization, net of tax	<b>1,517</b>	
Comprehensive income (loss)	<b>\$32,203</b>	\$(23,067)

## 12. INVENTORIES

Inventories, net of reserves, were as follows:

<i>In thousands</i>	<b>September 30, 2007</b>	December 31, 2006
Raw materials	<b>\$ 39,359</b>	\$ 38,539
In-process and finished	<b>97,075</b>	107,811
Supplies	<b>49,074</b>	45,931
Total	<b>\$185,508</b>	\$192,281

**13. LONG-TERM DEBT**

Long-term debt is summarized as follows:

<i>In thousands</i>	<b>September 30, 2007</b>	December 31, 2006
Revolving credit facility, due April 2011	<b>\$ 45,097</b>	\$ 64,795
Term loan, due April 2011	<b>73,000</b>	96,000
7 <sup>1</sup> / <sub>8</sub> % Notes, due May 2016	<b>200,000</b>	200,000
Note payable SunTrust, due March 2008	<b>34,000</b>	34,000
Total long-term debt	<b>352,097</b>	394,795
Less current portion <sup>(1)</sup>	<b>(49,532)</b>	(19,500)
Long-term debt, excluding current portion	<b>\$302,565</b>	\$375,295

<sup>(1)</sup> Includes \$34 million Note payable SunTrust. Refer to the separate discussion of intentions to extend this instrument's maturity.

Our revolving credit facility provides for up to \$200 million of aggregate borrowings on an unsecured basis. Our term loan requires quarterly repayments of principal that began on March 31, 2007 with the final principal payment due on April 2, 2011. In addition, if certain prepayment events occur, such as a sale of assets or the incurrence of additional indebtedness, as defined in the debt agreement, in excess of \$10.0 million in the

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aggregate, we must repay a specified portion of the term loan within five days of the prepayment event.

Borrowings under the credit agreement bear interest, at our option, at either (a) the bank's base rate described in the credit agreement as the greater of the prime rate or the federal funds rate plus 50 basis points, or (b) the EURO rate based generally on the London Interbank Offer Rate, plus an applicable margin that varies from 67.5 basis points to 137.5 basis points depending on our corporate credit rating determined by S&P and Moody's.

In June 2007, we negotiated an amendment to our credit agreement (the "Amended Credit Agreement") which, among other items increased the maximum leverage ratio for each fiscal quarter beginning June 30, 2007 and through and including March 31, 2008. The Amended Credit Agreement contains a number of customary covenants for financings of this type that, among other things, restrict our ability to: i) dispose of or create liens on assets; ii) transfer assets between borrowing or guaranteeing subsidiaries and non guaranteeing subsidiaries; iii) incur additional indebtedness; iv) repay other indebtedness; or v) make acquisitions and engage in mergers or consolidations. We are also required to comply with specified financial tests and ratios, each as defined in the Amended Credit Agreement, including a consolidated minimum net worth test and a maximum debt to earnings before interest, taxes, depreciation and amortization (EBITDA) ratio. A breach of these requirements, of which there were none at September 30, 2007, would give rise to certain remedies under the Amended Credit Agreement, among which are the termination of the agreement and accelerated repayment of the outstanding borrowings plus accrued and unpaid interest under the credit facility.

The 7<sup>1/8</sup>% Senior Note agreement contains a cross-default clause that provides if there were to be an event of default under the credit agreement discussed earlier, we would also be in default under the 7<sup>1/8</sup>% Senior Note.

Our outstanding debt obligations include a \$34 million Note Payable to SunTrust Financial (the "Note Payable"), all of which is presented in the accompanying condensed consolidated balance sheets as currently payable as of September 30, 2007. The Note Payable bears interest at a fixed rate of 3.82% for five years through March 2008, at which time we can elect to renew the obligation. The Note Payable relates to the March 2003 sale of approximately 25,500 acres of timberlands for which we received as consideration a \$37.9 million 10-year interest bearing note receivable from the timberland buyer. The note receivable is recorded as "Other assets" in the accompanying consolidated balance sheet. We pledged this note as collateral under the Note Payable. The debt agreement underlying this obligation

provides for an extension of the maturity of the Note Payable for up to five years assuming certain conditions are satisfied, all of which we believe to be, or will be, complied with. We intend to utilize the debt maturity extension clauses provided for in the original note agreement to extend the maturity of the Note Payable to March 2013.

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

As of September 30, 2007 and December 31, 2006, we had \$14.1 million and \$8.1 million in letters of credit issued to us by financial institutions. The letters of credit are for the benefit of government agencies in the Fox River environmental matter and certain state workers compensation insurance agencies in conjunction with our self-insurance program. No amounts were outstanding under the letters of credit. We bear the credit risk on this amount to the extent that we do not comply with the provisions of certain agreements. Outstanding letters of credit reduce amounts available under our revolving credit facility.

#### **14. SALE OF TIMBERLANDS**

On August 8, 2007, we entered into a definitive agreement to sell approximately 26,000 acres of timberlands to Glawson Investments Corp. ("Glawson"), a Georgia corporation, and GIC Investments LLC, a Delaware limited liability company owned by Glawson (the "Buyer") for approximately \$43.1 million, subject to certain adjustments. As consideration for the timberlands, at closing we are to receive a LIBOR-based interest bearing, 20-year installment note payable at maturity. The note will be fully secured by an irrevocable letter of credit. The transaction is expected to close in the fourth quarter of 2007. Upon closing, we expect to record a pre-tax gain approximating \$38 million.

In connection with the Agreement, at closing there under, the Buyers and us will enter into a 10-year Stumpage Agreement, pursuant to which we will agree to purchase and Glawson commits to sell an annual amount of standing timber approximating 73,860 tons per annum for the first 5 years and 55,755 tons per annum for the next five years thereafter. The price paid will be based on market rates for comparable timber and will be reset every six months.

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## 15. COMMITMENTS, CONTINGENCIES AND LEGAL PROCEEDINGS

### Fox River Neenah, Wisconsin

#### Background

We have significant uncertainties associated with environmental claims arising out of the presence of polychlorinated biphenyls ( PCBs ) in sediments in the lower Fox River and in the Bay of Green Bay. As part of the 1979 acquisition of the Bergstrom Paper Company we acquired a facility located at this site (the Neenah Facility ). In part, this facility used wastepaper as a source of fiber. At no time did the Neenah Facility utilize PCBs in the pulp and paper making process, but discharges to the Fox River from the facility which may have contained PCBs from wastepaper may have occurred from 1954 to the late 1970s. Any PCBs that the Neenah Facility discharged into the Fox River resulted from the presence of PCBs in NCR®-brand carbonless copy paper in the wastepaper that was received from others and recycled. We closed the Neenah Facility in June 2006.

As described below, various state and federal governmental agencies have formally notified nine potentially responsible parties ( PRPs ), including us, that they are potentially responsible for response costs and natural resource damages ( NRDs ) arising from PCB contamination at this site under the Comprehensive Environmental Response, Compensation and Liability Act ( CERCLA ) and other statutes. The other identified PRPs are NCR Corporation, Appleton Paper Inc., Georgia Pacific Corp. (formerly Fort Howard Corp. and Fort James Operating Company), WTM I Company ( WTM I , a subsidiary of Chesapeake Corp.), Riverside Paper Corporation, U.S. Paper Mills Corp. (a subsidiary of Sonoco Products Company), Sonoco Products Company, Menasha Corporation, and the U.S. Army Corps of Engineers.

The United States, on behalf of certain governmental authorities, is pursuing responsible parties to remediate the contaminated areas of the Fox River, to satisfy Natural Resource Damage claims, and to reimburse the governmental authorities for past costs. The areas of the lower Fox River and in the Bay of Green Bay in which PCB contamination exists are commonly referred to as Operable Unit 1 ( OU1 ), which consists of Little Lake Butte des Morts, the portion of the river that is closest to the Neenah Facility, Operable Unit 2 ( OU2 ), which is the portion of the river between dams at Appleton and Little Rapids, and Operable Units 3 through 5 ( OU3-5 ), an area approximately 20 miles downstream from the Neenah Facility.

CERCLA establishes a two-part liability structure that makes responsible parties liable for (1) response costs or response actions associated with the remediation of a release of hazardous substances and (2) NRDs related to that release. Courts have interpreted CERCLA to impose strict, joint and several liability on responsible parties for response costs, subject to equitable allocation in certain instances. Prior to a final settlement by all responsible parties and the final cleanup of the contamination, uncertainty regarding the application of that liability will persist.

The following table summarizes the potential range of costs to satisfy total claims associated with the Fox River matter based on the best available estimates. Such amounts are not necessarily indicative of our share of responsibility:

<i>In millions</i>	<b>Low</b>	<b>High</b>
OU1	\$ 93	\$ 137
OU2		
OU3 OU5	270	499
Natural Resource Damages (NRD)	76	333

OU1 is currently the only area of the Fox River in which we are conducting remediation activities. The high end of the range for OU1 set forth above assumes dredging of contamination as opposed to the use of alternative remedies. Based on discussions to date, we believe dredging the entire OU1 is remote. As discussed in detail below, our revised final plan assumes the use of alternative remedies. To date, approximately \$57 million of escrowed funds have been spent on OU1 remediation. The range of costs for OU3-5 is based on the cost of \$390 million set forth in the amended ROD issued in June 2007 plus or minus a 30% contingency factor. The range of NRD is based on recently obtained information that indicated \$76 million represents the best estimate of NRDs.

**Reserves for Fox River Environmental Liabilities**

We have reserves for existing environmental liabilities and for those environmental matters for which it is probable that a claim will be made and for which the amount of the obligation is reasonably estimable. The following table summarizes information with respect to such reserves.

<i>In millions</i>	<b>September 30, 2007</b>	December 31, 2006
<i>Recorded as:</i>		
Environmental liabilities	<b>\$ 8.7</b>	\$ 5.5
Other long-term liabilities	<b>20.0</b>	2.2
Total	<b>\$ 28.7</b>	\$ 7.7

With respect to the amounts set forth above, the caption "environmental liabilities" on the consolidated balance sheet represents the current portion of our reserves. Such classification is based on our best estimate.

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as to when the liability is expected to require the use of funds to settle the underlying obligation. As discussed later in this disclosure, during the first nine months of 2007, we recorded additional charges of \$26.0 million associated with the Fox River matter in our results of operations.

The following summarizes the status of our potential exposure:

***Response Actions and Recent Activities***

**OU1 and OU2** On January 7, 2003, the Wisconsin Department of Natural Resources (the Wisconsin DNR) and the Environmental Protection Agency (EPA) issued a Record of Decision (ROD) for the cleanup of OU1 and OU2. Subject to extenuating circumstances and alternative solutions provided for in the ROD, the ROD requires the removal of approximately 784,000 cubic yards of sediment from OU1 and no active remediation of OU2. The ROD also requires the long term monitoring of the two operable units. On July 1, 2003, WTM I Company entered into an Administrative Order on Consent (AOC) with EPA and the Wisconsin DNR regarding the implementation of the Remedial Design for OU1.

In the first quarter of 2004, the United States District Court for the Eastern District of Wisconsin approved a consent decree regarding OU1 (the OU1 Consent Decree). Under terms of the OU1 Consent Decree, we and WTM I each agreed to pay approximately \$27 million, of which \$25.0 million from each was placed in escrow to fund response work at OU-1 (OU-1 Escrow Account). The remaining amount that the parties agreed to pay under the Consent Decree includes payments for NRD and NRD assessment and other past costs incurred by the governments. In addition, the EPA agreed to contribute \$10 million from another settlement to the OU1 Escrow Account for the OU1 cleanup. As a result of these contributions, the total amount of funds initially available for remediation totaled \$60 million.

The terms of the OU1 Consent Decree restrict the use of the escrowed funds to qualifying remediation activities or restoration activities at the lower Fox River site. The response work is being performed by us and WTM I, with governmental oversight, and funded by the funds placed in the OU1 Escrow Account. Beginning in mid 2004, we and WTM I have performed activities to remediate OU1, including, among others, construction of de-watering and water-treatment facilities, dredging of portions of OU1, dewatering of the dredged materials, and hauling of the dewatered sediment to an authorized disposal facility.

The terms of the OU1 Consent Decree include provisions to be followed should the OU1 Escrow Account be depleted prior to completion of the response work. In this event, each settling company would be notified and be provided an opportunity to contribute additional funds to the OU1 Escrow Account. Should the OU1 Consent Decree be terminated due to insufficient funds, each settling company would lose the protections contained in the OU1 Consent Decree, and the governments may order one or both parties to complete the required remedial activities for OU-1. The governments may issue a similar order to a third party or perform the work themselves and seek response costs from any or all PRPs for the site, including us. If the OU1 Consent Decree is terminated due to the insufficiency of the escrow funds, we and WTM I would each remain potentially responsible for the costs necessary to complete the remedial action.

Since the start of these activities in the third quarter of 2004, approximately 320,000 cubic yards of contaminated sediment has been dredged.

**Recent activity** In late 2006, Glatfelter and WTM I jointly submitted a proposed Final Plan for the completion of the remediation of OU1 (the Final Plan) to Wisconsin DNR and EPA. The Final Plan proposed the implementation of permitted alternative remedies that require acceptance by the agencies. The cost estimates for the Final Plan were within the available funds.

Throughout 2007, we and WTM I have been actively engaged in discussions with the government agencies concerning the Final Plan. The Final Plan includes the use of engineered capping of certain areas in the river as opposed to dredging sediment. In the first quarter of 2007, after reviewing the refined cost estimates for the OU1 remediation and our projected estimates of the funds that would be available in the OU1 Escrow Account to implement the Final Plan, the governments notified us and WTM I that EPA was considering making a formal determination that the balance remaining in the OU1 Escrow Account was likely to be insufficient to fund the completion of the OU1 Remediation. We refined our cost estimates and as a result, the estimate of total costs to implement the Final Plan (including work already performed) increased. As a result of the revised cost estimate to

complete the remedy of OU1, we increased our reserve by \$6.0 million. We and WTM I agreed to address that potential shortfall in the OU1 Escrow Account by executing a supplement to the OU1 Consent Decree which provided that we each would commit to an additional \$6.0 million into the OU1 Escrow Account.

Subsequently, and as discussed below in June 2007 the agencies issued an amended Second ROD for OU3-5 which included the use of alternative remedies similar to, but more extensive than, those in the proposed Final Plan. In

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addition, during the third quarter of 2007 the agencies informed us that they would require capping or dredging in large portions of OU1 that we and WTM1 had proposed in the Final Plan would not be remediated due to the relatively low levels of contamination. As a result, we and WTM 1 have submitted a proposed revised Final Plan to the agencies that is consistent with the agencies' new requirements. As a result of applying the specifications of the agencies' requirements, the estimated costs to complete the OU1 remedies increased.

In October 2007, we and WTM I reached an agreement with another PRP under which this PRP will deposit \$7 million to the OU1 Escrow Account to secure performance of the remediation work in OU1 that is currently planned for 2008 (the PRP's Funds), assuming that that work can be performed at the expected cost. The PRP will provide the funds on an interim basis, and there is no agreement that the amounts provided either equal or exceed the PRP's fair share of costs to be incurred in OU1.

In the third quarter 2007, we conducted a pilot project to validate certain aspects of the Final Plan, including evaluating the engineered capping of contaminated areas. The impact of the revised cost estimates discussed above, the agreement with the PRP for additional funding and the estimated impact of other developments discussed above regarding the site, are all reflected in the additional \$20 million charge taken in the third quarter of 2007.

Based on information currently available to us, subject to i) government approval of the revised Final Plan proposed by us and WTM I; ii) the successful negotiation of acceptable and cost-effective contracts to complete the proposed remediation activities; and iii) effective implementation of the chosen technologies by the remediation contractor, and together with anticipated earnings on the funds currently on deposit in the escrow account and other assets available, we believe the required OU1 remedial actions can be completed for amounts reserved as of September 30, 2007.

**OUs 3-5** On July 28, 2003, the EPA and the Wisconsin DNR issued a ROD (the OU3-5 ROD) for the cleanup of OU3-5. The OU3-5 ROD calls for the removal of 6.5 million cubic yards of sediment and certain monitoring at an estimated cost of \$324.4 million but could, according to the OU3-5 ROD, cost within a range from approximately \$227.0 million to \$486.6 million. The most significant component of the estimated costs is attributable to large-scale sediment removal by dredging.

During the first quarter of 2004, NCR Corp. and Georgia Pacific Corp. entered into an AOC with the United States EPA under which they agreed to perform the Remedial Design for OU3-5. After gathering samples to perform the Remedial Design for OU3-5, elevated concentrations of PCBs were identified in sediments along the west bank of OU4, just downstream of the DePere Dam. Subsequently, during the second quarter of 2006, the United States filed a proposed Consent Decree with the U.S. District Court for the Eastern District of Wisconsin, under which NCR Corp. and Sonoco-U.S. Mills agreed to perform certain response actions regarding these sediments, on an expedited basis. In the spring of 2007, NCR Corp and Sonoco-U.S. Mills commenced this work.

**Recent Activity** In February 2007, we, along with the other PRPs involved in the OU2 and OU3-5 matters, received a General Notice Letter from the EPA requesting that each PRP advise the EPA of their willingness to discuss their liability for the costs to remediate OU2-5 and to provide a good faith offer to settle by April 1, 2007. Since the receipt of this letter, the recipients have had discussions to explore a potential settlement of the asserted claims. In an attempt to resolve their disputes concerning allocation of liability, we, together with several PRPs, have agreed to participate in non-binding mediation. The mediation, so far, has not resulted in any agreement as to allocation but is continuing. We do not know at this time whether an agreement will be reached between the governments and any PRPs to complete the remediation of OU2-5.

In June 2007, the EPA and the Wisconsin DNR issued an amendment to the OU3-5 ROD (the Amended OU3-5 ROD) that primarily, among other matters, expanded the Remedial Design provided for under the original ROD to include the use of engineered caps as an alternative to dredging. The Amended OU3-5 ROD estimates the total projected costs to be approximately \$385 million.

**Natural Resource Damages** Neither the ROD nor the OU3-5 ROD place any value on claims for NRDs associated with this matter. As noted above, NRD claims are distinct from costs related to the primary remediation of a Superfund site. Calculating the value of NRD claims is difficult, especially in the absence of a completed remedy for the underlying contamination. The State of Wisconsin, the United States Fish and Wildlife Service

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( FWS ), the National Oceanic and Atmospheric Administration ( NOAA ), four Indian tribes and the Michigan Attorney General have asserted that they possess NRD claims related to the lower Fox River and the Bay of Green Bay.

In September 1994, FWS notified the then-identified PRPs that it considered them potentially responsible for NRDs. The federal, tribal and Michigan agencies claiming to be NRD trustees have proceeded with the preparation of an NRD assessment. While the final assessment has yet to be completed, the federal trustees released a plan on October 25, 2000 that values NRDs for injured natural resources that allegedly fall under their trusteeship at between \$176 million and \$333 million. We believe that the federal NRD assessment is technically and procedurally flawed. We also believe that the NRD claims alleged by the various alleged trustees are legally and factually without merit.

The OU1 Consent Decree required that Glatfelter and WTM I each pay the governments \$1.5 million for NRDs for the Fox River site, and \$150,000 for NRD assessment costs. Each of these payments was made in return for credit to be applied toward each settling company's potential liability for NRDs associated with the Fox River site.

**Reserves for the Fox River Site** As of September 30, 2007 the OU1 Escrow Account balance totaled \$7.7 million, of which our portion totaled approximately \$1.6 million. This amount is recorded in the accompanying Consolidated Balance Sheet under the caption Prepaid expenses and other current assets. In addition to the Escrow Account balance, as discussed above, another PRP has agreed to contribute \$7 million to the Escrow Account and we and WTM I each have committed to provide an additional \$6 million towards OU1 remediation. Our committed share is recorded in the accompanying Consolidated Balance Sheet under the caption Environmental liabilities.

As a result of the recent developments concerning the Fox River including: (i) our revised cost estimates for the Final Plan; (ii) developments in the ongoing PRP mediation and discussions with other PRPs; and (iii) the stated intentions of Wisconsin DNR and EPA; we have recorded an additional charge of \$20 million in the third quarter 2007 to satisfy our current obligations at OU1 and all pending, threatened or asserted and unasserted claims against us for the Fox River including OU3-5. This additional charge represents our current assessment of the ultimate costs to be incurred by us associated with the revised Final Plan and any settlement of NRDs and OU 3-5 exposures. As of September 30, 2007, our reserve for the Fox River environmental liability totaled \$28.7 million. Our reserve includes amounts originally established in 2003 and adjustments in the first and third quarter of 2007 increasing the liability by \$6 million and \$20 million, respectively, offset by expenditures related to remediation activities.

The EPA has stated its intention to issue one or more unilateral administrative orders ( UAO ) for performance of the work required by the Amended OU3-5 ROD. We do not yet know whether any UAOs will be issued, if so, when they will be issued, and, if issued, what they will require of us or of others.

We contend that we do not have any liability for remediation of OU3-5 because we believe that we have strong defenses to liability including that there is ample credible data that indicates that PCBs did not leave OU1 in concentrations that could have caused or contributed to the need for cleanup more than 20 miles downstream in OU3-5. Others, including the EPA and other PRPs, disagree with us and, as a result, the EPA could issue some group of PRPs, including us, a UAO to perform the OU3-5 work or this matter could otherwise result in litigation. Even if we are not successful in establishing our non-liability for OU3-5, we do not believe that we would be allocated a significant percentage share of liability in any equitable allocation of the remediation costs and other potential damages associated with OU3-5. The accompanying consolidated financial statements do not include reserves for any future litigation or defense costs for the Fox River, and should litigation be necessary, the costs to do so could be significant. If we are ordered to complete more than what we believe to be our fair share of any remediation efforts, the costs to do so could be significant.

Other than with respect to the OU1 Consent Decree, the amount and timing of future expenditures for environmental compliance, cleanup, remediation and personal injury, NRDs and property damage liabilities cannot be ascertained with any certainty due to, among other things, the unknown extent and nature of any contamination, the extent and timing of any technological advances for pollution abatement, the response actions that may be required, the availability of qualified remediation contractors, equipment, and landfill space, and the number and financial resources of any other PRPs.

**Other Information** The Wisconsin DNR and FWS have each published studies, the latter in draft form, estimating the amount of PCBs discharged by each identified PRP to the lower Fox River and the Bay of Green Bay. These

reports estimate the Neenah Facility's share of the volumetric discharge to be as high as 27%. We do not believe the volumetric estimates used in these studies are accurate because (a) the studies themselves disclose that they are not accurate and (b) the volumetric estimates contained in the studies are based on assumptions that are unsupported by existing evidence. We believe that our volumetric contribution is significantly lower than the estimates set forth in these studies. Further, we do not believe that a volumetric allocation would constitute an equitable distribution of the potential liability for the contamination. Other factors,

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such as the location of contamination, the location of discharge, and a party's role in causing discharge, must be considered in order for the allocation to be equitable.

We have entered into interim cost-sharing agreements with four of the other PRPs, pursuant to which such PRPs have agreed to share both defense costs and costs for scientific studies relating to PCBs discharged into the lower Fox River. These interim cost-sharing agreements have no bearing on the final allocation of costs related to this matter. Based upon our evaluation of the magnitude, nature and location of the various discharges of PCBs to the river and the relationship of those discharges to identified contamination, we believe our share of any liability among the identified PRPs is much less than our per capita share of the cost sharing agreement.

We also believe that there exist additional potentially responsible parties other than the identified PRPs. For instance, certain of the identified PRPs discharged their wastewater through public wastewater treatment facilities, which we believe makes the owners of such facilities potentially responsible in this matter. We also believe that entities providing PCB-containing wastepaper to each of the recycling mills are also potentially responsible in this matter.

While the OU1 Consent Decree, as amended, provides a negotiated framework for resolving both our and WTM I's liability for the remediation of OU1, it may not completely resolve our exposure at the Fox River. We anticipate this matter may result in litigation but cannot predict the timing, nature, magnitude or outcome of such litigation.

**Range of Reasonably Possible Outcomes** Our analysis of the range of reasonably possible outcomes is derived from all available information, including but not limited to official documents such as RODs, discussions with governments and other PRPs, as well as legal counsel and engineering consultants. Based on our analysis of currently available information and experience regarding the cleanup of hazardous substances, we believe that it is reasonably possible that our costs associated with the Fox River matter discussed herein may exceed the amount of charges taken by amounts that may prove to be insignificant or that could range, in the aggregate, up to approximately \$120 million, over a period that is undeterminable but that could range beyond 15 years. We believe that the likelihood of an outcome in the upper end of the monetary range is significantly less than other possible outcomes within the range and that the possibility of an outcome in excess of the upper end of the monetary range is remote.

In our estimate of the upper end of the range of reasonable possible outcomes for the entire river, we have considered: (i) the remedial actions agreed upon to date under the OU1 Consent Decree; (ii) our understanding of the Amended OU3-5 ROD; and (iii) no current requirement for any active remediation of OU2. We have also assumed successful implementation of the Amended OU3-5 ROD, although at a significantly higher cost than estimated in the Amended OU3-5 ROD. We have also assumed our share of the ultimate liability to be 18%, which is significantly higher than we believe is appropriate or than we will incur, and a level of NRD claims and claims for reimbursement of expenses from other parties that, although reasonably possible, is unlikely.

Based on currently available information, including actual remediation costs incurred to date, we believe that the remediation of OU1 as proposed in our revised Final Plan can be completed with available amounts in the OU1 Escrow Account, the amounts committed to be funded and the amounts currently reserved. Our assessment assumes that: 1) the revised Final Plan will be approved by the governments; 2) we and WTM I successfully negotiate acceptable contracts to complete remediation activities; and 3) the OU1 remediation contractor will successfully implement the revised Final Plan. However, if we are unsuccessful in managing our costs to implement the revised Final Plan additional charges may be necessary and such amounts could be material.

The OU1 Consent Decree does not address response costs necessary to remediate the remainder of the Fox River site and only addresses NRDs and claims for reimbursement of government expenses to a limited extent. Because CERCLA imposes strict joint and several liability, uncertainty persists regarding our exposure with respect to the remainder of the Fox River site.

In estimating both our current reserves for environmental remediation and other environmental liabilities and the possible range of costs, we have assumed that we will not bear the entire cost of remediation and damages to the exclusion of other known PRPs who may be jointly and severally liable. The ability of other PRPs to participate has been taken into account, generally based on their financial condition and probable contribution. Our evaluation of the other PRPs' financial condition included the review of publicly available financial information. Furthermore, we believe certain of these PRPs have corporate or contractual relationships with additional entities that may shift to those

entities some or all of the monetary obligations arising from the Fox River site. The relative probable contribution is based upon our knowledge that at least two PRPs manufactured the paper, and arranged for the disposal of the wastepaper,

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that included the PCBs and consequently, in our opinion, bear a higher level of responsibility.

In addition, our assessment is based upon the magnitude, nature and location of the various discharges of PCBs to the river and the relationship of those discharges to identified contamination. We will continue to evaluate our exposure and the level of our reserves, including, but not limited to, our potential share of the costs and NRDs, if any, associated with the Fox River site.

**Summary** Our current assessment is that we should be able to manage these environmental matters without a long-term, material adverse impact on the Company. These matters could, however, at any particular time or for any particular year or years, have a material adverse effect on our consolidated financial position, liquidity and/or results of operations or could result in a default under our loan covenants. Moreover, there can be no assurance that our reserves will be adequate to provide for future obligations related to these matters, that our share of costs and/or damages for these matters will not exceed our available resources, or that such obligations will not have a long-term, material adverse effect on our consolidated financial position, liquidity or results of operations. With regard to the Fox River site, if we are not successful in managing the implementation of the OU1 Consent Decree and/or if we are ordered to implement the remedy proposed in the Amended OU3-5 ROD, such developments could have a material adverse effect on our consolidated financial position, liquidity and results of operations and may result in a default under our loan covenants.

#### **Ecusta Division Matters**

At September 30, 2007, we had reserves for various matters associated with our former Ecusta Division. Summarized below is the activity in these reserves during the period indicated:

<i>In thousands</i>	Ecusta Environmental Matters	Workers Comp	Other	Total
Balance, Jan. 1, 2007	\$7,202	\$1,409		\$ 8,611
Payments	(817)	(683)		(1,500)
Balance, Sept 30, 2007	\$6,385	\$ 726		\$ 7,111
Balance, Jan. 1, 2006	\$8,105	\$1,913	\$ 3,300	\$13,318
Payments	(673)	(262)	(3,262)	(4,197)
Other Adjustments			(38)	(38)
Balance, Sept 30, 2006	\$7,432	\$1,651	\$	\$ 9,083

With respect to the reserves set forth above as of September 30, 2007, \$1.1 million is recorded under the caption Other current liabilities and \$6.0 million is recorded under the caption Other long-term liabilities in the accompanying condensed consolidated balance sheets.

The following discussion provides more details on each of these matters.

**Background Information** In August 2001, pursuant to an acquisition agreement (the Acquisition Agreement), we sold the assets of our Ecusta Division to four related entities, consisting of Purico (IOM) Limited, an Isle of Man limited liability company (Purico), RF&Son Inc. (RF), RFS US Inc. (RFS US) and RFS Ecusta Inc. (RFS Ecusta), each of which is a Delaware corporation (collectively, the Buyers).

In August 2002, the Buyers shut down the manufacturing operation of the pulp and paper mill in Pisgah Forest, North Carolina, which was the most significant operation of the Ecusta Division. On October 23, 2002, RFS Ecusta and RFS US (the Debtors) separately filed for bankruptcy under Chapter 11 of the U.S. Bankruptcy Code. The bankruptcy cases were later converted to Chapter 7 proceedings. Effective August 8, 2003, the assets of RFS Ecusta and RFS US, which substantially consist of the pulp and paper mill and related real property, were sold to several

third parties unrelated to the Buyers (the New Buyers ).

***Ecusta Environmental Matters*** Beginning in April 2003, government authorities, including the North Carolina Department of Environment and Natural Resources ( NCDENR ), initiated discussions with us and the New Buyers regarding, among other environmental issues, certain landfill closure liabilities associated with the Ecusta mill and its properties. The discussions focused on NCDENR 's desire to establish a plan and secure financial resources to close three landfills located at the Ecusta facility and to address other environmental matters at the facility. During the third quarter of 2003, the discussions ended with NCDENR 's conclusion to hold us responsible for the closure of three landfills. Accordingly, we established reserves approximating \$7.6 million representing estimated closure costs. In March 2004 and September 2005, the NCDENR issued us separate orders requiring the closure of two of the three landfills at issue. We have completed the closure of these two landfills and are in the process of closing the third.

In October 2004, one of the New Buyers entered into a Brownfields Agreement with the NCDENR relating to the Ecusta mill, pursuant to which the New Buyers were to be held responsible for certain specified environmental issues at the Ecusta Facility.

In September 2005, NCDENR sought our participation, pursuant to a proposed consent order, in the

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evaluation and potential remediation of environmentally hazardous conditions at the former Ecusta mill site. In January 2006, NCDENR modified its proposed consent order to include us and the company (the Prior Owner ) from whom our predecessor, Ecusta Corporation, purchased the Ecusta mill. NCDENR and the United States Environmental Protection Agency ( USEPA ) have indicated that if neither party enters into a consent order USEPA intends to list the mill site on the National Priorities List and pursue assessment and remediation of the site under the Comprehensive Environmental Responsibility, Compensation and Liability Act (more commonly known as Superfund ). In addition to calling for the assessment, closure, and post-closure monitoring and maintenance of the third landfill for which we since have been directed to close, the proposed consent order would impose an obligation to assess and remediate the following:

- i. mercury and certain other contamination on and around the site;
- ii. potentially hazardous conditions existing in the sediment and water column of the site s water treatment and aeration and sedimentation basin (the ASB ); and
- iii. contamination associated with two additional landfills on the site that were not used by us.

With respect to the concerns set forth above (collectively, the NCDENR matters ), we contend that the Prior Owner is responsible for any mercury contamination at the Ecusta Facility and that the New Buyers, as owner and operator of the ASB, are responsible for addressing any issues associated with the ASB, including closure, and that the New Buyers, in a May 2004 agreement, expressly agreed to indemnify and hold us harmless from certain environmental liabilities, which include most, if not all, of the NCDENR matters. We continue to have discussions with NCDENR and USEPA concerning our potential responsibilities and appropriate remedial actions, if any, which may be necessary.

The Prior Owners of the site have filed a declaratory judgment action in the US District Court that seeks a determination by the Court that, under the Purchase Agreement pursuant to which the Ecusta Facility was conveyed to Glatfelter, Glatfelter is obligated to indemnify the Prior Owners for any costs related to the remediation of mercury contamination at the Ecusta Facility. In response, Glatfelter has filed an answer denying that it is responsible for such costs and a counterclaim against the Prior Owners alleging, among others things, fraud and negligent misrepresentation by the Prior Owner regarding mercury contamination. We continue to evaluate potential legal claims we may have with respect to Prior Owners and other parties with respect to any remediation of hazardous substance that may be ultimately required at the Ecusta Facility.

As a result of NCDENR s September 2005 communication with us and our assessment of the range of likely outcomes of the NCDENR Matters and the New Buyers Matters, our results of operations for 2005 included a \$2.7 million charge to increase our reserve for estimated costs associated with the Ecusta environmental matters. The addition to the reserve includes estimated operating costs associated with the obligations of the New Buyer discussed above, estimated costs to perform an assessment of certain risks posed by the presence of mercury, further characterization of sediment in the ASB and treatment of other contamination. Since this initial accrual, no further changes have been made.

The 2005 reserves relating to additional environmental assessment activities were premised, in part, on the belief that it might be mutually beneficial to us and NCDENR if we were to agree to perform the assessment activities, without accepting responsibility for any subsequently required remediation. While it now appears clear that NCDENR and USEPA will not accept such an arrangement, it is uncertain in the absence of a consent order i) what actions will be taken by the agencies; ii) against whom any such actions may be taken; and iii) when any additional remediation would be required to be performed.

In addition, it is unclear how the liability for any required assessment or remediation will be apportioned among the Prior Owner, Glatfelter, the Buyers and the New Buyers. We are also in negotiations with potential buyers of the Ecusta Facility (the Potential Buyers ) and the New Buyers concerning the division of assessment and remediation obligations for known and suspected contamination at the Ecusta Facility and certain off-site areas between us and the Potential Buyers. However, the outcome of these negotiations is uncertain. For the foregoing reasons, in part, our recorded reserve does not include costs associated with further remediation activities that we may be required to

perform, the range of which we are currently unable to estimate; however, they could be significant.

We are evaluating options presented to us by the Potential Buyers, including proposals for Glatfelter, the Prior Owner and the Potential Buyers to jointly contribute to the cost to remediate any on-site contamination. To date we believe we are adequately reserved to participate in such an arrangement at the level currently proposed; however, there are no assurances that we will reach agreement with the Potential Buyers and the Prior Owner on the terms of such an arrangement. We are uncertain as to what additional Ecusta-related claims, including, among others, environmental matters, government

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oversight and government past costs, if any, may be asserted against us

It is possible that the New Buyers may not have sufficient cash flow from their operations to satisfy certain ongoing obligations to NCDENR and us and, their ability to do so may be dependent on their ability to sell the Ecusta Facility. Specifically, the New Buyers are obligated (i) to treat leachate and stormwater runoff from the landfills, which we are currently required to manage, and (ii) to pump and treat contaminated groundwater in the vicinity of a former caustic building at the site. If the New Buyers should default on these obligations, it is possible that NCDENR will require us to make appropriate arrangements for these obligations and to be responsible for the remediation of certain contamination on and around the site (collectively, the New Buyers Matters ). We continue to discuss with the New Buyers and the Potential Buyers the need for assurances that the New Buyers or the Potential Buyers, or both, will fulfill the New Buyers obligations for the New Buyers Matters.

Notwithstanding a potential sale of the property, and with respect to alleged mercury contamination at the site, i) the extent of mercury contamination is unknown; ii) it is unclear who will be required to remediate this contamination; and iii) the ultimate costs to remedy such contamination are not reasonably estimable based on information currently available to us. Accordingly, no amounts to address such contamination have been included in our reserve discussed above. If we are required to perform additional remediation at the Ecusta Facility, additional charges would be required, and such amounts could be material.

**Workers Compensation** Prior to 2003, we established reserves related to potential workers compensation claims associated with the former Ecusta Division, which at that time were estimated to total approximately \$2.2 million. In the fourth quarter of 2005, the North Carolina courts issued a ruling that held us liable for workers compensation claims of certain employees injured during their employment at the Ecusta facility prior to our sale of the Division. Since this ruling, we have made payments as indicated in the reserve analysis presented earlier in this Note 15.

In addition to the specific matters discussed above, we are subject to loss contingencies resulting from regulation by various federal, state, local and foreign governments with respect to the environmental impact of our mills. To comply with environmental laws and regulations, we have incurred substantial capital and operating expenditures in past years. We anticipate that environmental regulation of our operations will continue to become more burdensome and that capital and operating expenditures necessary to comply with environmental regulations will continue, and perhaps increase, in the future. In addition, we may incur obligations to remove or mitigate the adverse effects, if any, on the environment resulting from our operations, including the restoration of natural resources and liability for personal injury and for damages to property and natural resources.

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

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**16. SEGMENT AND GEOGRAPHIC INFORMATION**

The following table sets forth financial and other information by business unit for the periods indicated:

<b>Business Unit Performance</b>	For The Three Months Ended September 30,							
	Specialty Papers		Composite Fibers		Other and Unallocated		Total	
<i>In thousands</i>	2007	2006	2007	2006	2007	2006	2007	2006
Net sales	\$207,894	\$202,096	\$83,965	\$75,393	\$	\$	\$291,859	\$277,489
Energy sales, net	2,491	2,706					2,491	2,706
Total revenue	210,385	204,802	83,965	75,393			294,350	280,195
Cost of products sold	180,739	183,364	68,327	62,240	(1,596)	(3,312)	247,470	242,292
Gross profit (loss)	29,646	21,438	15,638	13,153	1,596	3,312	46,880	37,903
SG&A	14,988	11,374	7,452	8,023	19,757	5,193	42,197	24,590
Shutdown and restructuring charges						2,222		2,222
Gains on dispositions of plant, equipment and timberlands					(2,301)	(923)	(2,301)	(923)
Gain on insurance recoveries								
Total operating income (loss)	14,658	10,064	8,186	5,130	(15,860)	(3,180)	6,984	12,014
Nonoperating income (expense)					(6,477)	(5,750)	(6,477)	(5,750)
Income (loss) before income taxes	\$ 14,658	\$ 10,064	\$ 8,186	\$ 5,130	\$ (22,337)	\$ (8,930)	\$ 507	\$ 6,264
<b>Supplementary Data</b>								
Net tons sold	190,505	180,365	17,823	17,919			208,328	198,284
Depreciation and depletion expense	\$ 9,084	\$ 8,133	\$ 5,345	\$ 4,344	\$	\$	\$ 14,429	\$ 12,477
<b>Business Unit Performance</b>	For The Nine Months Ended September 30,							
<i>In thousands</i>	Specialty Papers		Composite Fibers		Other and Unallocated		Total	
	2007	2006	2007	2006	2007	2006	2007	2006
Net sales	\$607,404	\$507,906	\$253,535	\$209,909			\$860,939	\$717,815
Energy sales, net	7,129	8,010					7,129	8,010
Total revenue	614,533	515,916	253,535	209,909			868,068	725,825
Cost of products sold	551,476	469,857	209,639	177,962	(5,436)	14,105	755,679	661,924
Gross profit (loss)	63,057	46,059	43,896	31,947	5,436	(14,105)	112,389	63,901
SG&A	44,036	35,361	23,946	20,608	26,718	10,358	94,700	66,327

Shutdown and restructuring charges					<b>162</b>	28,177	<b>162</b>	28,177
Gains on dispositions of plant, equipment and timberlands					<b>(11,188)</b>	(2,008)	<b>(11,188)</b>	(2,008)
Gain on insurance recoveries						(205)		(205)
Total operating income (loss)	<b>19,021</b>	10,698	<b>19,950</b>	11,339	<b>(10,256)</b>	(50,427)	<b>28,715</b>	(28,390)
Nonoperating income (expense)					<b>(19,382)</b>	(16,065)	<b>(19,382)</b>	(16,065)
Income (loss) before income taxes	<b>\$ 19,021</b>	\$ 10,698	<b>\$ 19,950</b>	\$ 11,339	<b>\$ (29,638)</b>	\$(66,492)	<b>\$ 9,333</b>	\$(44,455)
<b>Supplementary Data</b>								
Net tons sold	<b>548,969</b>	488,305	<b>54,298</b>	50,471		10	<b>603,267</b>	538,786
Depreciation and depletion expense	<b>\$ 26,615</b>	\$ 24,487	<b>\$ 15,678</b>	\$ 12,635			<b>\$ 42,293</b>	\$ 37,122

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

Management evaluates results of operations of the business units before non-cash pension income, charges related to the Fox River environmental reserves, restructuring related charges, unusual items, effects of asset dispositions and insurance recoveries because it believes this is a more meaningful representation of the operating performance of its core papermaking businesses, the profitability of business units and the extent of cash flow generated from core operations. Such amounts are presented above under the caption Other and Unallocated. This presentation is closely aligned with the management and operating structure of our company. It is also on this basis that the Company's performance is evaluated internally and by the Company's Board of Directors.

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**17. GUARANTOR FINANCIAL STATEMENTS**

Our 7<sup>1</sup>/<sub>8</sub>% Senior Notes have been fully and unconditionally guaranteed, on a joint and several basis, by certain of our 100%-owned domestic subsidiaries, PHG Tea Leaves, Inc., Mollanvick, Inc., The Glatfelter Pulp Wood Company, GLT International Finance, LLC, Glatfelter Holdings, LLC and Glatfelter Holdings II, LLC.

The following presents our condensed consolidating statements of income, cash flow and our condensed consolidating balance sheets for the periods indicated. These financial statements reflect P. H. Glatfelter Company (the parent), the guarantor subsidiaries (on a combined basis), the non-guarantor subsidiaries (on a combined basis) and elimination entries necessary to combine such entities on a consolidated basis.

During 2007, we completed a reorganization pursuant to which, Glenn Wolfe was merged into the parent company. Accordingly the 2007 financial information set forth below reflects such reorganization. All prior period financial information has been restated.

**Condensed Consolidating Statement of Income for the  
three months ended September 30, 2007**

<i>In thousand</i>	Parent Company	Guarantors	Non Guarantors	Adjustments/ Eliminations	Consolidated
Net sales	\$207,895	\$ 10,765	\$83,964	\$ (10,765)	\$291,859
Energy sales net	2,491				2,491
Total revenues	210,386	10,765	\$83,964	(10,765)	294,350
Costs of products sold	179,508	(10,376)	68,466	(10,880)	247,470
Gross profit	30,878	389	15,498	115	46,880
Selling, general and administrative expenses	33,712	567	7,918		42,197
Shutdown and restructuring charges	89		(89)		
Gains on dispositions of plant, equipment and timberlands, net	(138)	(2,154)	(9)		(2,301)
Gains from insurance recoveries					
Operating income	(2,785)	1,976	7,678	115	6,984
Non-operating income (expense)					
Interest expense	(7,051)	(1)	(517)		(7,569)
Other income (expense) net	12,239	4,153	(1,685)	(13,615)	1,092
Total other income (expense)	5,188	4,152	(2,202)	(13,615)	(6,477)
Income (loss) before income taxes	2,403	6,128	5,476	(13,500)	507
Income tax provision (benefit)	(5,409)	2,138	(3,466)	(568)	(7,305)
Net income (loss)	\$ 7,812	\$ 3,990	\$ 8,942	\$(12,932)	\$ 7,812

**Condensed Consolidating Statement of Income for the three  
months ended September 30, 2006**



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<i>In thousand</i>	Parent Company	Guarantors	Non Guarantors	Adjustments/ Eliminations	Consolidated
Net sales	\$202,096	\$8,834	\$75,393	\$(8,834)	\$277,489
Energy sales net	2,706				2,706
Total revenues	204,802	8,834	75,393	(8,834)	280,195
Costs of products sold	180,521	8,577	61,795	(8,601)	242,292
Gross profit	24,281	257	13,598	(233)	37,903
Selling, general and administrative expenses	15,982	563	8,045		24,590
Shutdown and restructuring charges	2,181		41		2,222
Gains on dispositions of plant, equipment and timberlands, net	(664)	(514)	255		(923)
Gains from insurance recoveries					
Operating income	6,782	208	5,257	(233)	12,014
Non-operating income (expense)					
Interest expense	(5,888)		(1,124)		(7,012)
Other income (expense) net	5,279	3,848	(1,484)	(6,381)	1,262
Total other income (expense)	(609)	3,848	(2,608)	(6,381)	(5,750)
Income (loss) before income taxes	6,173	4,056	2,649	(6,614)	6,264
Income tax provision (benefit)	805	1,423	(108)	(1,224)	896
Net income (loss)	\$ 5,368	\$2,633	\$ 2,757	\$(5,390)	\$ 5,368

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**Condensed Consolidating Statement of Income for the  
nine months ended September 30, 2007**

<i>In thousand</i>	Parent Company	Guarantors	Non Guarantors	Adjustments/ Eliminations	Consolidated
Net sales	\$ 607,406	\$ 32,368	\$ 253,533	\$ (32,368)	\$ 860,939
Energy sales net	7,129				7,129
Total revenues	614,535	32,368	253,533	(32,368)	868,068
Costs of products sold	548,180	29,829	210,002	(32,332)	755,679
Gross profit	66,355	2,539	43,531	(36)	112,389
Selling, general and administrative expenses	67,578	1,675	25,447		94,700
Shutdown and restructuring charges	262		(100)		162
Gains on dispositions of plant, equipment and timberlands, net	41	(11,220)	(9)		(11,188)
Gains from insurance recoveries					
Operating income	(1,526)	12,084	18,193	(36)	28,715
Non-operating income (expense)					
Interest expense	(20,653)	(1)	(1,676)		(22,330)
Other income (expense) net	25,821	11,727	(4,278)	(30,322)	2,948
Total other income (expense)	5,168	11,726	(5,954)	(30,322)	(19,382)
Income (loss) before income taxes	3,642	23,810	12,239	(30,358)	9,333
Income tax provision (benefit)	(9,421)	9,148	(1,590)	(1,867)	(3,730)
Net income (loss)	\$ 13,063	\$ 14,662	\$ 13,829	\$ (28,491)	\$ 13,063

**Condensed Consolidating Statement of Income for the  
nine months ended September 30, 2006**

<i>In thousand</i>	Parent Company	Guarantors	Non Guarantors	Adjustments/ Eliminations	Consolidated
Net sales	\$ 507,905	\$ 27,041	\$ 209,910	\$ (27,041)	\$ 717,815
Energy sales net	8,010				8,010
Total revenues	515,915	27,041	209,910	(27,041)	725,825
Costs of products sold	485,929	24,775	177,793	(26,573)	661,924
Gross profit	29,986	2,266	32,117	(468)	63,901

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Selling, general and administrative expenses	43,231	1,989	21,107		66,327
Shutdown and restructuring charges	28,056		121		28,177
Gains on dispositions of plant, equipment and timberlands, net	(584)	(1,716)	292		(2,008)
Gains from insurance recoveries	(205)				(205)
Operating income	(40,512)	1,993	10,597	(468)	(28,390)
Non-operating income (expense)					
Interest expense	(14,845)	(463)	(2,267)		(17,575)
Other income (expense) net	7,619	10,903	(3,410)	(13,602)	1,510
Total other income (expense)	(7,226)	10,440	(5,677)	(13,602)	(16,065)
Income (loss) before income taxes	(47,738)	12,433	4,920	(14,070)	(44,455)
Income tax provision (benefit)	(20,521)	4,593	671	(1,981)	(17,238)
Net income (loss)	\$ (27,217)	\$ 7,840	\$ 4,249	\$ (12,089)	\$ (27,217)

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**Condensed Consolidating Balance Sheet as of September 30, 2007**

<i>In thousands</i>	Parent Company	Guarantors	Non Guarantors	Adjustments/ Eliminations	Consolidated
<b>Assets</b>					
<b>Current assets</b>					
Cash and cash equivalents	\$ 3,386	\$ 284	\$ 14,150	\$	\$ 17,820
Other current assets	332,566	327,087	39,740	(345,353)	354,040
Plant, equipment and timberlands net	290,240	12,524	216,652		519,416
Other assets	707,963	153,093	(68,815)	(463,184)	329,057
Total assets	\$1,334,155	\$492,988	\$201,727	\$(808,537)	\$1,220,333
<b>Liabilities and Shareholders</b>					
<b>Equity</b>					
Current liabilities	\$ 381,467	\$ 81,802	\$ 97,540	\$(342,901)	\$ 217,908
Long-term debt	302,565				302,565
Deferred income taxes	135,928	17,348	28,405	(16,292)	165,389
Other long-term liabilities	102,957	5,179	7,903	7,194	123,233
Total liabilities	922,917	104,329	133,848	(351,999)	809,095
Shareholders equity	411,238	388,659	67,879	(456,538)	411,238
Total liabilities and shareholders equity	\$1,334,155	\$492,988	\$201,727	\$(808,537)	\$1,220,333

**Condensed Consolidating Balance Sheet as of December 31, 2006**

<i>In thousands</i>	Parent Company	Guarantors	Non Guarantors	Adjustments/ Eliminations	Consolidated
<b>Assets</b>					
<b>Current assets</b>					
Cash and cash equivalents	\$ 10,227	\$ 546	\$ 11,212	\$	\$ 21,985
Other current assets	234,038	10,083	114,983	(6,051)	353,053
Plant, equipment and timberlands net	302,606	12,945	213,316		528,867
Other assets	1,269,299	475,354	(153,452)	(1,269,463)	321,738
Total assets	\$1,816,170	\$498,928	\$ 186,059	\$(1,275,514)	\$1,225,643
<b>Liabilities and Shareholders</b>					
<b>Equity</b>					

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Current liabilities	\$ 157,029	\$ 2,753	\$ 36,375	\$ (2,867)	\$ 193,290
Long-term debt	329,516		45,779		375,295
Deferred income taxes	137,180	18,112	29,472	(2,105)	182,659
Other long-term liabilities	804,077	91,418	25,844	(835,308)	86,031
Total liabilities	1,427,802	112,283	137,470	(840,280)	837,275
Shareholders' equity	388,368	386,645	48,589	(435,234)	388,368
Total liabilities and shareholders' equity	\$1,816,170	\$498,928	\$ 186,059	\$(1,275,514)	\$1,225,643

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**Condensed Consolidating Statement of Cash Flows for the  
nine months ended September 30, 2007**

<i>In thousands</i>	Parent Company	Guarantors	Non Guarantors	Adjustments/ Eliminations	Consolidated
Net cash provided (used) by Operating Activities	\$ 47,891	\$(11,109)	\$ 20,981	\$	\$ 57,763
Investing Activities					
Purchase of plant, equipment and timberlands	(13,279)	(800)	(5,210)		(19,289)
Proceeds from disposal plant, equipment and timberlands	242	11,647	210		12,099
Acquisition of Lydney mill and Chillicothe					
Total Investing Activities	(13,037)	10,847	(5,000)		(7,190)
Financing Activities					
Net (repayments of) proceeds from indebtedness	(31,571)		(13,852)		(45,423)
Payment of Dividends	(12,253)				(12,253)
Proceeds from Stock Options exercised	1,477				1,477
Total Financing Activities	(42,347)		(13,852)		(56,199)
Effect of Exchange Rate on Cash	652		809		1,461
Net Increase (decrease) in cash	(6,841)	(262)	2,938		(4,165)
Cash at the beginning of period	10,227	546	11,212		21,985
Cash at the end of period	\$ 3,386	\$ 284	\$ 14,150	\$	\$ 17,820

**Condensed Consolidating Statement of Cash Flows for the  
nine months ended September 30, 2006**

<i>In thousands</i>	Parent Company	Guarantors	Non Guarantors	Adjustments/ Eliminations	Consolidated
Net cash provided (used) by Operating Activities	\$ (65,649)	\$ 39,953	\$(20,611)	\$ (33)	\$ (46,340)
Investing Activities					
Purchase of plant, equipment and timberlands	(29,259)	(999)	(4,967)		(35,225)
Proceeds from disposal plant, equipment and timberlands	2,921	51	3		2,975
Acquisition of Lydney mill and Chillicothe	(89,211)	(68,937)			(158,148)

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Total Investing Activities	(115,549)	(69,885)	(4,964)		(190,398)
Financing Activities					
Net (repayments of) proceeds from indebtedness	170,354		27,499		197,853
Payment of Dividends	(11,993)				(11,993)
Proceeds from Stock Options exercised	8,090				8,090
Total Financing Activities	166,451		27,499		193,950
Effect of Exchange Rate on Cash			(773)		(773)
Net Increase (decrease) in cash	(14,747)	(29,932)	1,151	(33)	(43,561)
Cash at the beginning of period	14,524	30,495	12,390	33	57,442
Cash at the end of period	\$ (223)	\$ 563	\$ 13,541	\$	\$ 13,881

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## ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

*The following discussion should be read in conjunction with the information in the unaudited condensed consolidated financial statements and notes thereto included herein and Glatfelter's Financial Statements and Management's Discussion and Analysis of Financial Condition and Results of Operations included in its 2006 Annual Report on Form 10-K.*

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

- i. variations in demand for, or pricing of, our products;
- ii. changes in the cost or availability of raw materials we use, in particular pulpwood, market pulp, pulp substitutes, and abaca fiber, and changes in energy-related costs;
- iii. our ability to develop new, high value-added Specialty Papers and Composite Fibers products;
- iv. the impact of competition, changes in industry paper production capacity, including the construction of new mills, the closing of mills and incremental changes due to capital expenditures or productivity increases;
- v. our ability to successfully and cost effectively operate the recently acquired Chillicothe and Lydney facilities;
- vi. cost and other effects of environmental compliance, cleanup, damages, remediation or restoration, or personal injury or property damages related thereto, such as the costs of natural resource restoration or damages related to the presence of polychlorinated biphenyls ( PCBs ) in the lower Fox River on which our former Neenah mill was located; and the costs of environmental matters at our former Ecusta Division mill;
- vii. the gain or loss of significant customers and/or on-going viability of such customers;
- viii. risks associated with our international operations, including local economic and political environments and fluctuations in currency exchange rates;
- ix. geopolitical events, including war and terrorism;
- x. enactment of adverse state, federal or foreign tax or other legislation or changes in government policy or regulation;
- xi. adverse results in litigation;
- xii. disruptions in production and/or increased costs due to labor disputes or contract negotiations;
- xiii. our ability to successfully execute our timberland strategy to realize the value of our timberlands; and



xiv. our ability to finance, consummate and integrate future acquisitions.

**Introduction** We manufacture, both domestically and internationally, a wide array of specialty papers and engineered products. Substantially all of our revenue is earned from the sale of our products to customers in numerous markets, including book publishing, envelope and converting, carbonless papers and forms, food and beverage, decorative laminates for furniture and flooring, and other highly technical niche markets.

**Overview** Our results of operations for the first nine months and for the third quarter of 2007 when compared to the same periods of 2006 reflect stronger performance from each of our business units. Domestically, the Specialty Papers business unit's results, in the comparison, are positively influenced by the improved productivity of the Chillicothe and Spring Grove facilities and by additional volumes associated with the April 2006 Chillicothe acquisition.

Our Composite Fibers business unit's results have been positively influenced by additional volumes associated with the Lydney acquisition that was completed in March 2006 as well as improved mix. Average selling prices on a constant currency basis improved in the comparison.

The comparison of year-to-date results are affected by the completion of the business acquisitions referenced earlier which includes; i) the \$65 million acquisition of J R Crompton's Lydney mill on March 13, 2006; and ii) the \$83.3 million acquisition of Chillicothe, the carbonless paper operation of NewPage Corporation. In connection with the Chillicothe acquisition, effective June 30, 2006 we ceased production at our Neenah, WI facility and transferred those products, including the production of book paper, to Chillicothe.

The results of operations in the first nine months of 2007 include \$26 million of pre-tax charges, \$20.0 million of which were recorded in the third quarter, related to our estimated costs associated with the Fox River environmental matter. The results also include approximately \$5.3 million of income tax benefits recorded as a result of a change in the corporate income tax rate in Germany.

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**RESULTS OF OPERATIONS****Nine Months Ended September 30, 2007 versus  
the Nine Months Ended September 30, 2006**

The following table sets forth summarized results of operations:

<i>In thousands, except per share</i>	<b>Nine Months Ended September 30</b>	
	<b>2007</b>	<b>2006</b>
Net sales	<b>\$860,939</b>	\$717,815
Gross profit	<b>112,389</b>	63,901
Operating income (loss)	<b>28,715</b>	(28,390)
Net income (loss)	<b>13,063</b>	(27,217)
Earnings per share	<b>0.29</b>	(0.61)

The consolidated results of operations for the nine months ended September 30, 2007 and 2006 includes the following significant items:

<i>In thousands, except per share</i>	<b>2007</b>	<b>After-tax</b>	<b>Diluted EPS</b>
		<i>Gain (loss)</i>	
Environmental remediation		<b>\$(15,979)</b>	<b>\$ (0.35)</b>
Acquisition integration related costs		<b>(1,472)</b>	<b>(0.03)</b>
Timberland sales		<b>6,815</b>	<b>0.15</b>
	<b>2006</b>		
Shutdown and restructuring charges		\$(34,034)	\$ (0.76)
Acquisition integration related costs		(6,817)	(0.15)
Debt redemption premium		(1,820)	(0.04)
Timberland sales		832	0.02
Insurance recoveries		130	

The above items decreased earnings by \$10.6 million, or \$0.23 per diluted share in the first nine months of 2007. In the comparable period a year ago, the above items decreased earnings by \$41.7 million, or \$0.93 per diluted share.

**Business Units**

<b>Business Unit Performance</b> <i>In thousands</i>	For the Nine Months Ended September 30,							
	Specialty Papers		Composite Fibers		Other and Unallocated		Total	
	<b>2007</b>	2006	<b>2007</b>	2006	<b>2007</b>	2006	<b>2007</b>	2006
Net sales	<b>\$607,404</b>	\$507,906	<b>\$253,535</b>	\$209,909			<b>\$860,939</b>	\$717,815
Energy sales, net	<b>7,129</b>	8,010					<b>7,129</b>	8,010
Total revenue	<b>614,533</b>	515,916	<b>253,535</b>	209,909			<b>868,068</b>	725,825
Cost of products sold	<b>551,476</b>	469,857	<b>209,639</b>	177,962	<b>(5,436)</b>	14,105	<b>755,679</b>	661,924
Gross profit (loss)	<b>63,057</b>	46,059	<b>43,896</b>	31,947	<b>5,436</b>	(14,105)	<b>112,389</b>	63,901

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SG&A	<b>44,036</b>	35,361	<b>23,946</b>	20,608	<b>26,718</b>	10,358	<b>94,700</b>	66,327
Shutdown and restructuring charges					<b>162</b>	28,177	<b>162</b>	28,177
Gains on dispositions of plant, equipment and timberlands					<b>(11,188)</b>	(2,008)	<b>(11,188)</b>	(2,008)
Gain on insurance recoveries						(205)		(205)
Total operating income (loss)	<b>19,021</b>	10,698	<b>19,950</b>	11,339	<b>(10,256)</b>	(50,427)	<b>28,715</b>	(28,390)
Nonoperating income (expense)					<b>(19,382)</b>	(16,065)	<b>(19,382)</b>	(16,065)
Income (loss) before income taxes	<b>\$ 19,021</b>	\$ 10,698	<b>\$ 19,950</b>	\$ 11,339	<b>\$(29,638)</b>	\$(66,492)	<b>\$ 9,333</b>	\$ (44,455)
<b>Supplementary Data</b>								
Net tons sold	<b>548,969</b>	488,305	<b>54,298</b>	50,471		10	<b>603,267</b>	538,786
Depreciation and depletion expense	<b>\$ 26,615</b>	\$ 24,487	<b>\$ 15,678</b>	\$ 12,635			<b>\$ 42,293</b>	\$ 37,122

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**Sales and Costs of Products Sold**

<i>In thousands</i>	Nine Months Ended September 30		Change
	2007	2006	
Net sales	<b>\$860,939</b>	\$717,815	\$143,124
Energy sales net	<b>7,129</b>	8,010	(881)
Total revenues	<b>868,068</b>	725,825	142,243
Costs of products sold	<b>755,679</b>	661,924	93,755
Gross profit	<b>\$112,389</b>	\$63,901	\$48,488
Gross profit as a percent of Net sales	<b>13.1%</b>	8.9%	

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

<b>Business Unit</b>	Percent of Total	
	2007	2006
Specialty Papers	<b>70.6%</b>	70.8%
Composite Fibers	<b>29.4</b>	29.2
Total	<b>100.0%</b>	100.0%

Net sales totaled \$860.9 million for the first nine months of 2007, an increase of \$143.1 million, or 19.9%, compared to the same period a year ago.

In the Specialty Papers business unit, net sales increased \$99.5 million to \$607.4 million. The increase is largely attributable to the Chillicothe acquisition that was completed April 3, 2006. In addition, an overall favorable pricing environment resulted in a \$13.9 million benefit in the first nine months of 2007 with prices increasing in all product markets. Shipping volumes increased 12.4% in the comparison. Specialty Papers production costs increased in the comparison, primarily due to material usage and lower machine yields on book publishing products. In addition, raw material prices increased by approximately \$11.3 million largely driven by wood, pulp, coal and energy.

In Composite Fibers, net sales were \$253.5 million for the first nine months of 2007, up \$43.6 million from the prior-year period. The completion of the March 13, 2006 Lydney acquisition accounted for approximately \$17.5 million of the increase. On a constant currency basis, average selling prices increased on average 1.8% and volumes increased approximately 7.6% with increases seen in food and beverage, technical specialties and metalized product markets. Energy and raw material costs in this business unit were \$3.3 million higher than a year ago. Costs of products sold for the first nine months of 2007 include a \$1.4 million benefit from an energy tax credit and from an insurance recovery related to a 2005 event.

The 2006 costs of products sold includes a \$25.7 million charge for inventory write-downs and accelerated depreciation on property and equipment abandoned in connection with the Neenah facility shutdown.

**Non-Cash Pension Income** Non-cash pension income results from the over-funded status of our pension plans. The amount of pension income recognized each year is determined using various actuarial assumptions and certain other factors, including the fair value of our pension assets as of the beginning of the year. The following summarizes non-cash pension income, before the curtailment charges recorded in connection with the Neenah shutdown during 2006:

<i>In thousands</i>	Nine Months Ended September 30		Change
	2007	2006	
<i>Recorded as:</i>			
Costs of products sold	<b>\$6,473</b>	\$11,545	\$(5,072)
SG&A expense	<b>3,173</b>	1,099	2,074
Total	<b>\$9,646</b>	\$12,644	\$(2,998)

**Selling, general and administrative ( SG&A )** expenses increased \$28.4 million in the period-to-period comparison and totaled \$94.7 million for the first nine months of 2007. The increase was due to a \$26.0 million charge for the Fox River environmental matter and the inclusion of a full year's results for the Chillicothe and Lydney acquisitions in the current period's results. These unfavorable factors were partially offset in the comparison by lower acquisition integration costs.

**Gain on Sales of Plant, Equipment and Timberlands** During the first nine months of 2007 and 2006, gains on dispositions of plant, equipment and timberlands totaled \$11.2 million and \$2.0 million, respectively. Such gains are primarily from the completion of sales of timberlands which are summarized by the following table:

<i>Dollars in thousands</i>	Acres	Proceeds	Gain
2007	<b>4,674</b>	<b>\$11,649</b>	<b>\$11,223</b>
2006	465	1,573	1,503

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**Shutdown and Restructuring Charges – Neenah Facility Shutdown** In connection with our agreement to acquire the Chillicothe operations, we committed to a plan to permanently close the Neenah, WI facility. Production at this facility ceased effective June 30, 2006 and certain products previously manufactured at the Neenah facility have been transferred to Chillicothe.

During the first nine months of 2007, we increased our reserve for costs associated with the shutdown by \$0.3 million and made payments totaling \$1.6 million; thus, the remaining reserve balance was \$1.5 million at September 30, 2007.

The results of operations in the first nine months of 2006 include the following pre-tax charges related to the Neenah shutdown:

<i>In thousands</i>	Nine Months Ended September 30, 2006
Accelerated depreciation	\$ 22,457
Inventory write-down	3,196
Severance and benefit continuation	7,219
Pension and other retirement benefits curtailments	7,675
Contract termination costs	11,367
Other	1,795
<b>Total</b>	<b>\$ 53,709</b>

With the exception of the severance and benefit continuation amounts and contract termination costs, substantially all other amounts accrued represent either accelerated non-cash asset write-downs or costs expected to be paid for from the Company's overfunded pension plan.

As part of the Neenah shutdown, we terminated our long-term steam supply contract, as provided for within the contract, resulting in an accrued termination fee of approximately \$11.4 million.

The Neenah shutdown resulted in the elimination of approximately 200 positions that had been supporting our Specialty Papers business unit. Approximately \$24.9 million of the Neenah shutdown related charges are recorded as part of costs of products sold in the accompanying statements of income. The amounts accrued for severance and benefit continuation are recorded as other current liabilities in the accompanying consolidated balance sheets.

**Income taxes** For the first nine months of 2007, we recorded a benefit for income taxes totaling \$3.7 million on pre tax income of \$9.3 million. The 2007 income tax benefits include a \$5.3 million deferred income tax benefit related to the reduction of German corporate income tax passed into law July 2007.

**Foreign Currency** We own and operate paper and pulp mills in Germany, France, the United Kingdom and the Philippines. The functional currency in Germany and France is the Euro, in the UK the British Pound Sterling, and in the Philippines the currency is the Peso. During the first nine months of 2007, Euro functional currency operations generated approximately 19.6% of our sales and 18.4% of operating expenses and British Pound Sterling operations represented 7.2% of net sales and 7.3% of operating expenses. The translation of the results from these international operations into U.S. dollars is subject to changes in foreign currency exchange rates.

The table below summarizes the impact on reported results that changes in currency exchange rates in the current year period compared with the prior year period had on our non-U.S. based operations from the conversion of these operation's non-U.S. dollar denominated revenues and expenses into U.S. dollars.

Nine Months  
Ended

In thousands	September 30
	<b>Favorable</b>
	<b>(unfavorable)</b>
Net sales	\$ 15,797
Costs of products sold	(16,566)
SG&A expenses	(1,476)
Income taxes and other	(109)
Net income	\$ (2,354)

The above table only presents the financial reporting impact of foreign currency translations. It does not present the impact of certain competitive advantages or disadvantages of operating or competing in multi-currency markets.

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**Three Months Ended September 30, 2007 versus the  
Three Months Ended September 30, 2006**

The following table sets forth summarized results of operations:

<i>In thousands, except per share</i>	Three Months Ended September 30	
	2007	2006
Net sales	<b>\$291,859</b>	\$277,489
Gross profit	<b>46,880</b>	37,903
Operating income	<b>6,984</b>	12,014
Net income (loss)	<b>7,812</b>	5,368
Earnings (loss) per share	<b>0.17</b>	0.12

The consolidated results of operations for the three months ended September 30, 2007 includes the following significant items:

<i>In thousands, except per share</i>	2007	After-tax	Diluted EPS
		<i>Gain (loss)</i>	
Environmental remediation		<b>\$(12,286)</b>	<b>\$(0.27)</b>
Acquisition integration related costs		<b>(322)</b>	<b>(0.01)</b>
Timberland sales		<b>1,415</b>	<b>0.03</b>
	2006		
Shutdown and restructuring charges		\$ (1,904)	\$ (0.04)
Acquisition integration related costs		(3,560)	(0.08)
Redemption premium			
Timberland sales		250	

**Business Units** The following table sets forth profitability information by business unit and the composition of consolidated income before income taxes:

<b>Business Unit Performance</b> <i>In thousands, except net tons sold</i>	For the Three Months Ended September 30, Other and							
	Specialty Papers		Composite Fibers		Unallocated		Total	
	2007	2006	2007	2006	2007	2006	2007	2006
Net sales	<b>\$207,894</b>	\$202,096	<b>\$83,965</b>	\$75,393	\$	\$	<b>\$291,859</b>	\$277,489
Energy sales, net	<b>2,491</b>	2,706					<b>2,491</b>	2,706
Total revenue	<b>210,385</b>	204,802	<b>83,965</b>	75,393			<b>294,350</b>	280,195
Cost of products sold	<b>180,739</b>	183,364	<b>68,327</b>	62,240	<b>(1,596)</b>	(3,312)	<b>247,470</b>	242,292
Gross profit (loss)	<b>29,646</b>	21,438	<b>15,638</b>	13,153	<b>1,596</b>	3,312	<b>46,880</b>	37,903
SG&A	<b>14,988</b>	11,374	<b>7,452</b>	8,023	<b>19,757</b>	5,193	<b>42,197</b>	24,590
						2,222		2,222



Shutdown and restructuring charges								
Gains on dispositions of plant, equipment and timberlands					(2,301)	(923)	(2,301)	(923)
Gain on insurance recoveries								
Total operating income (loss)	<b>14,658</b>	10,064	<b>8,186</b>	5,130	<b>(15,860)</b>	(3,180)	<b>6,984</b>	12,014
Non-operating income (expense)					<b>(6,477)</b>	(5,750)	<b>(6,477)</b>	(5,750)
Income (loss) before income taxes	<b>\$ 14,658</b>	\$ 10,064	<b>\$ 8,186</b>	\$ 5,130	<b>\$(22,337)</b>	\$(8,930)	<b>\$ 507</b>	\$ 6,264

**Supplementary Data**

Net tons sold	<b>190,505</b>	180,365	<b>17,823</b>	17,919			<b>208,328</b>	198,284
Depreciation and depletion expense	<b>\$ 9,084</b>	\$ 8,133	<b>\$ 5,345</b>	\$ 4,344	\$	\$	<b>\$ 14,429</b>	\$ 12,477

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The following table summarizes sales and costs of products sold for the three months ended September 30, 2007 and 2006.

### Sales and Costs of Products Sold

<i>In thousands</i>	Three Months Ended September 30		Change
	2007	2006	
Net sales	\$291,859	\$277,489	\$14,370
Energy sales net	2,491	2,706	(215)
Total revenues	294,350	280,195	14,155
Costs of products sold	247,470	242,292	5,178
Gross profit	\$ 46,880	\$ 37,903	\$ 8,977
Gross profit as a percent of Net sales	16.1%	13.7%	

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

<b>Business Unit</b>	Percent of Total	
	2007	2006
Specialty Papers	71.2%	72.8%
Composite Fibers	28.8	27.2
Total	100.0%	100.0%

Net sales totaled \$291.9 million for the third quarter of 2007, an increase of \$14.4 million, or approximately 5.2%, compared to the same period a year ago.

In the Specialty Papers business unit, net sales increased by \$5.8 million, or 2.9%. An overall favorable pricing environment resulted in a \$3.5 million benefit in the third quarter of 2007 compared with the same period of 2006 with prices increasing in all product markets. In addition, productivity improved at both of this business unit's facilities. These favorable factors were partially offset by \$5.7 million of higher raw material prices largely driven by wood, pulp and energy.

In Composite Fibers, net sales were \$84.0 million for the third quarter of 2007, up from \$8.6 million from the prior-year period. On a constant currency basis, average selling prices increased \$1.0 million and volumes were essentially flat in the comparison. Costs of products sold for the third quarter of 2007 include a \$1.4 million benefit from an energy tax credit and from an insurance recovery related to a 2005 event. Energy and raw material costs in this business unit were \$1.1 million higher than a year ago.

As discussed earlier, the 2006 costs of products sold includes a \$0.8 million charge for inventory write-downs in connection with the Neenah facility shutdown.

**Non-Cash Pension Income** Non-cash pension income results from the considerably over-funded status of our pension plans. The amount of pension income recognized each year is determined using various actuarial assumptions and certain other factors, including the fair value of our pension assets as of the beginning of the year. The following summarizes non-cash pension income for each quarter:

Three Months Ended

<i>In thousands</i>	September 30		Change
	2007	2006	
<i>Recorded as:</i>			
Costs of products sold	\$1,779	\$4,092	\$(2,313)
SG&A expense	1,446	586	860
Total	\$3,225	\$4,678	\$(1,453)

**Selling, general and administrative ( SG&A )** expenses increased \$17.6 million in the quarter-to-quarter comparison and totaled \$42.2 million in the third quarter of 2007. The increase was mainly due to a \$20.0 million charge to increase the reserve for Fox River environmental matters, partially offset by the absence of integration related costs incurred in the prior year quarter.

**Income taxes** For the third quarter of 2007, we recorded income tax benefits totaling \$7.3 million on pre tax income of \$0.5 million. The benefit is primarily due to a \$5.3 million deferred income tax benefit related to the reduction of the German corporate income tax passed into law July 2007. The balance of the benefit arises from the closure of certain tax years as well as the higher tax rate relating to our normal operating rate associated with the \$20 million charge for the environmental matters at the Fox River.

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**Foreign Currency** During the third quarter of 2007, Euro functional currency operations generated approximately 18.9% of our sales and 18.0% of operating expenses and British Pound Sterling operations represented 7.2% of net sales and 7.4% of operating expenses. The translation of the results from these international operations into U.S. dollars is subject to changes in foreign currency exchange rates.

The table below summarizes the impact on reported results that changes in currency exchange rates in the current year period compared with the prior year period had on our non-U.S. based operations from the conversion of these operations non-U.S. dollar denominated revenues and expenses into U.S. dollars.

<i>In thousands</i>	Three Months Ended September 30, 2007 Favorable (unfavorable)
Net sales	\$ 5,075
Costs of products sold	(5,468)
SG&A expenses	(514)
Income taxes and other	248
Net income	\$ (659)

The above table only presents the financial reporting impact of foreign currency translations. It does not present the impact of certain competitive advantages or disadvantages of operating or competing in multi-currency markets.

#### **LIQUIDITY AND CAPITAL RESOURCES**

Our business is capital intensive and requires expenditures for new or enhanced equipment, for environmental compliance matters and to support our business strategy and research and development efforts. The following table summarizes cash flow information for each of the periods presented.

<i>In thousands</i>	Nine Months Ended September 30	
	2007	2006
Cash and cash equivalents at beginning of period	\$ 21,985	\$ 57,442
Cash provided by (used for)		
Operating activities	57,763	(46,340)
Investing activities	(7,190)	(190,398)
Financing activities	(56,199)	193,950
Effect of exchange rate changes on cash	1,461	(773)
Net cash provided (used)	(4,165)	(43,561)
Cash and cash equivalents at end of period	\$ 17,820	\$ 13,881

Operating cash flow improved by \$104.1 million in the comparison primarily due to improved operating results together with improved working capital usage. In addition, cash used for operations in 2006 included \$21.7 million to settle a cross currency rate swap, \$17.4 million of income tax payments and \$15.4 million of cash paid for restructuring charges.

The changes in investing cash flows primarily reflect the use of approximately \$158.1 million in the first nine months of 2006 to fund the Lydney and Chillicothe acquisitions. Capital expenditures in the comparison declined \$15.9 million in the current year and totaled \$19.3 million.

During the first nine months of 2007 and 2006, cash dividends paid on common stock totaled approximately \$12.3 million and \$12.0 million, respectively. Our Board of Directors determines what, if any, dividends will be paid to our shareholders. Dividend payment decisions are based upon then-existing factors and conditions and, therefore, historical trends of dividend payments are not necessarily indicative of future payments.

During the first nine months of 2007, net debt declined \$40.2 million as proceeds from operations and timberland sales were used to reduce debt outstanding. In the year earlier period net borrowings of \$197.9 million were used to finance the Lydney and Chillicothe acquisitions.

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

<i>In thousands</i>	<b>September 30, 2007</b>	December 31, 2006
Revolving credit facility, due April 2011	<b>\$ 45,097</b>	\$ 64,795
Term loan, due April 2011	<b>73,000</b>	96,000
7 <sup>1</sup> / <sub>8</sub> % Notes, due May 2016	<b>200,000</b>	200,000
Note payable SunTrust, due March 2008	<b>34,000</b>	34,000
Total long-term debt	<b>352,097</b>	394,795
Less current portion	<b>(49,532)</b>	(19,500)
Long-term debt, excluding current portion	<b>\$302,565</b>	\$375,295

The significant terms of the debt obligations are set forth in Item 1 Financial Statements and Supplementary Data, Note 13.

We are subject to loss contingencies resulting from regulation by various federal, state, local and foreign governmental authorities with respect to the environmental impact of mills we operate, or have operated. To comply with environmental laws and regulations, we have incurred substantial capital and operating expenditures in past years. We anticipate that environmental regulation of our operations will continue to become more burdensome and that capital and operating expenditures necessary to comply with environmental regulations will continue, and perhaps increase, in the future. In addition, we may incur obligations to remove or mitigate any adverse effects on the environment resulting from our operations, including the restoration of natural resources and liability for personal injury and for damages to property and natural resources. See Item 1 Financial Statements Note 15 for a summary of significant environmental matters.

We expect to meet all of our near- and longer-term cash needs from a combination of operating cash flow, cash and cash equivalents, sales of timberland, our existing credit facility or other bank lines of credit and other long-term debt. However, as discussed in Item 1 Financial Statements Note 15, an unfavorable outcome of various environmental matters could have a material adverse impact on our consolidated financial position, liquidity and/or results of operations.

Our credit agreement, as amended, contains a number of customary compliance covenants. In addition, the 7<sup>1</sup>/<sub>8</sub>% Notes contain a cross default provision that in the event of a default under the credit agreement, the 7<sup>1</sup>/<sub>8</sub>% Notes would become currently due. As of September 30, 2007, we met all of the requirements of our debt covenants.

**Off-Balance-Sheet Arrangements** As of September 30, 2007 and December 31, 2006, we had not entered into any off-balance-sheet arrangements. Financial derivative instruments to which we are a party and guarantees of indebtedness, which solely consist of obligations of subsidiaries and a partnership, are reflected in the condensed consolidated balance sheets included herein in Item 1 Financial Statements.

**Outlook** We expect pricing in the Specialty Papers business unit to increase moderately over the next several quarters as a result of announced price increases in the marketplace. The benefits of higher selling prices are expected to be largely offset by the impact of higher input costs, particularly fiber and energy. Shipping volumes in this business unit for the fourth quarter of 2007 are expected to trend lower on a sequential quarter basis reflecting seasonally lower demand.

In Composite Fibers, average selling prices are expected to remain stable or increase slightly over the next several quarters. Volumes in the fourth quarter are expected to be flat in the quarter over quarter comparison.

### **ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISKS**

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<i>Dollars in thousands</i>	Year Ended December 31					At September 30, 2007	
	2007	2008	2009	2010	2011	Carrying Value	Fair Value
<b>Long-term debt</b>							
Average principal outstanding							
At fixed interest rates							
Bond	\$200,000	\$200,000	\$200,000	\$200,000	\$200,000	\$200,000	\$197,515
At fixed interest rate							
SunTrust Note	34,000	8,500				34,000	\$ 33,638
At variable interest rates	118,097	108,364	88,069	67,360	23,993	118,097	118,098
						\$352,097	\$349,250
Weighted-average interest rate							
On fixed interest rate debt	7.13%	7.13%	7.13%	7.13%	7.13%		
On fixed interest rate debt SunTrust Note	3.82	3.82					
On variable interest rate debt	6.24	6.26	6.32	6.41	6.46		

GLATFELTER

Our market risk exposure primarily results from changes in interest rates and currency exchange rates. At September 30, 2007, we had long-term debt outstanding of \$352.1 million, of which \$118.1 million or 33.5% was at variable interest rates.

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

Variable-rate debt outstanding represents borrowings under our revolving credit facility that incur interest based on the domestic prime rate or a Eurocurrency rate, at our option, plus a margin. At September 30, 2007, the interest rate paid was 6.24%. A hypothetical 100 basis point increase or decrease in the interest rate on variable rate debt would increase or decrease annual interest expense by \$1.2 million.

We are subject to certain risks associated with changes in foreign currency exchange rates to the extent our operations are conducted in currencies other than the U.S. Dollar. During the first nine months of 2007, Euro functional currency operations generated approximately 19.6% of our sales and 18.4 % of operating expenses and British Pound Sterling operations represented 7.2% of net sales and 7.3 % of operating expenses.

#### **ITEM 4. CONTROLS AND PROCEDURES**

**Evaluation of Disclosure Controls and Procedures** Our chief executive officer and our principal financial officer, after evaluating the effectiveness of our disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) as of September 30, 2007, have concluded that, as of the evaluation date, our disclosure controls and procedures are effective.

**Changes in Internal Controls** There were no changes in our internal control over financial reporting during the three months ended September 30, 2007, that have materially affected or are reasonably likely to materially affect our internal control over financial reporting.

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**PART II**

**ITEM 6. EXHIBITS**

The following exhibits are filed herewith.

- 10.1 Timberland Purchase & Sale Agreement - Virginia Timberlands, entered into by and between Glawson Investments Corp., GIC Investments LLC and Glatfelter Pulp Wood Company, dated and effective as of August 8, 2007.
- 31.1 Certification of George H. Glatfelter II, Chairman and Chief Executive Officer of Glatfelter, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2 Certification of John P. Jacunski, Senior Vice President and Chief Financial Officer of Glatfelter, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1 Certification of George H. Glatfelter II, Chairman and Chief Executive Officer of Glatfelter, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, 18 U.S.C. Section 1350.
- 32.2 Certification of John P. Jacunski, Senior Vice President and Chief Financial Officer of Glatfelter, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, 18 U.S.C. Section 1350.

**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

P. H. GLATFELTER COMPANY  
(Registrant)

November 9, 2007

By /s/ David C. Elder  
David C. Elder  
Corporate Controller

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**EXHIBIT INDEX**

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31.2	Certification of John P. Jacunski, Senior Vice President and Chief Financial Officer of Glatfelter, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 Chief Financial Officer, filed herewith.
32.1	Certification of George H. Glatfelter II, Chairman and Chief Executive Officer of Glatfelter, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 Chief Executive Officer, filed herewith.
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