UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the Quarterly Period Ended March 31, 2001

or

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

For the transition period from to ______________ to ______________

Commission file number 1-15399

PACKAGING CORPORATION OF AMERICA
(Exact Name of Registrant as Specified in its Charter)

Delaware (State or other Jurisdiction of Incorporation or Organization)	**36-4277050** (IRS Employer Identification No.)
1900 West Field Court **Lake Forest, Illinois** (Address of Principal Executive Offices)	**60045** (Zip Code)

(847) 482-3000
(Registrant's telephone number, including area code)

Not Applicable
(Former name, former address and former fiscal year, if changed since last report)

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

As of May 11, 2001, the Registrant had outstanding 106,637,794 shares of common stock, par value $0.01 per share.

PART I
FINANCIAL INFORMATION

Item 1. Financial Statements.

Packaging Corporation of America
Condensed Consolidated Balance Sheets

(In thousands, except share and per share amounts)	**March 31, 2001** **(unaudited)**	**December 31, 2000**
Assets		
Current assets:		
Cash and cash equivalents	$ 46,271	$ 7,892
Accounts and notes receivable, net of allowance for doubtful accounts of $5,855 and $6,394 as of March 31, 2001 and December 31, 2000, respectively	203,979	215,994
Inventories	153,259	159,712
Prepaid expenses and other current assets	11,373	5,755
Deferred income taxes	8,300	14,356
Total current assets	423,182	403,709
Property, plant and equipment, net	1,443,155	1,455,990
Intangible assets, net of accumulated amortization of $1,436 and $1,380 as of March 31, 2001 and December 31, 2000, respectively	1,701	1,758
Other long-term assets	78,785	80,655
Total assets	$1,946,823	$1,942,112
Liabilities and shareholders' equity		
Current liabilities:		
Current portion of long-term debt	$ 70	$ 239
Accounts payable	100,196	113,701
Accrued interest	26,589	15,438
Accrued liabilities	67,477	89,170
Total current liabilities	194,332	218,548
Long-term liabilities:		
Long-term debt	858,185	869,175
Deferred income taxes	161,035	151,728
Other liabilities	17,622	15,237
Total long-term liabilities	1,036,842	1,036,140
Shareholders' equity:		
Common stock (par value $.01 per share, 300,000,000 shares authorized, 106,569,762 shares and 106,248,138 shares issued as of March 31, 2001 and December 31, 2000, respectively)	1,065	1,062
Additional paid in capital	513,668	512,208
Retained earnings	202,087	174,468
Accumulated other comprehensive loss	(857)	—
Common stock held in treasury, at cost (27,470 shares at March 31, 2001 and December 31, 2000, respectively)	(314)	(314)
Total shareholders' equity	715,649	687,424
Total liabilities and shareholders' equity	$1,946,823	$1,942,112

See notes to consolidated financial statements.

Packaging Corporation of America

Condensed Consolidated Statements of Income

(unaudited)

(In thousands, except per share amounts)	Three Months Ended March 31, 2001	Three Months Ended March 31, 2000
Net sales	$ 454,666	$ 475,890
Cost of sales	(347,488)	(367,344)
Gross profit	107,178	108,546
Selling and administrative expenses	(30,642)	(29,083)
Other income (expense), net	(219)	2,867
Corporate overhead	(10,357)	(9,589)
Income before interest, taxes and cumulative effect of accounting change	65,960	72,741
Interest expense, net	(19,562)	(30,242)
Income before taxes and cumulative effect of accounting change	46,398	42,499
Provision for income taxes	(18,284)	(17,253)
Income before cumulative effect of accounting change	28,114	25,246
Cumulative effect of accounting change, net of tax	(495)	—
Net income	27,619	25,246
Preferred dividends and accretion of preferred stock issuance costs	—	(18,637)
Net income available to common shareholders	$ 27,619	$ 6,609
Weighted average common shares outstanding:		
Basic	106,414	101,583
Diluted	108,959	104,856
Basic earnings per common share:		
Income before cumulative effect of accounting change	$ 0.26	$ 0.07
Cumulative effect of change in accounting principle	—	—
Net income per common share	$ 0.26	$ 0.07
Diluted earnings per common share:		
Income before cumulative effect of accounting change	$ 0.25	$ 0.06
Cumulative effect of accounting change	—	—
Net income per common share	$ 0.25	$ 0.06

See notes to consolidated financial statements.

Packaging Corporation of America

Condensed Consolidated Statements of Cash Flows

(unaudited)

(In thousands)	Three Months Ended March 31, 2001	Three Months Ended March 31, 2000
Cash Flows from Operating Activities:		
Net income	$ 27,619	$ 25,246
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation, depletion and amortization	34,221	35,808
Amortization of financing costs	1,222	1,694
Cumulative effect of accounting change	495	—
Increase in deferred income taxes	16,234	12,547
Gain on disposal of property, plant and equipment	(587)	(635)
Other, net	418	(275)
Changes in components of working capital:		
(Increase) decrease in current assets—		
Accounts receivable	12,015	(10,330)
Inventories	6,453	3,512
Prepaid expenses and other	(5,618)	(448)
Decrease in current liabilities—		
Accounts payable	(13,505)	(12,900)
Accrued liabilities	(10,542)	(8,835)
Net cash provided by operating activities	68,425	45,384
Cash Flows from Investing Activities:		
Additions to property, plant and equipment	(20,049)	(19,606)
Additions to other long term assets	(1,346)	(1,724)
Proceeds from disposals of property, plant and equipment	878	1,508
Other, net	177	82
Net cash used for investing activities	(20,340)	(19,740)
Cash Flows from Financing Activities:		
Redemption of preferred stock	—	(124,432)
Payments on long-term debt	(11,169)	(13,756)
Proceeds from initial public offering	—	126,528
Issuance of common stock upon exercise of stock options	1,463	—
Net cash used for financing activities	(9,706)	(11,660)
Net Increase in Cash	38,379	13,984
Cash and cash equivalents, beginning of period	7,892	10,300
Cash and cash equivalents, end of period	$ 46,271	$ 24,284

See notes to consolidated financial statements.

Packaging Corporation of America

Notes to Condensed Consolidated Financial Statements

(unaudited)

March 31, 2001

1. Basis of Presentation

Packaging Corporation of America ("PCA" or the "Company") was incorporated on January 25, 1999 pursuant to the General Corporation Law of the State of Delaware. PCA was formed to acquire the containerboard and corrugated packaging products business (the "Group") of Pactiv Corporation, formerly known as Tenneco Packaging Inc., a wholly owned subsidiary of Tenneco Inc. PCA had no operations from the date of incorporation on January 25, 1999 to April 11, 1999.

On April 12, 1999, Pactiv Corporation ("Pactiv") sold the Group to PCA for $2.2 billion. The Group is the predecessor to PCA. The $2.2 billion purchase price paid to Pactiv for the Group consisted of $246.5 million in cash, the assumption of $1.8 billion of debt incurred by Pactiv immediately prior to closing, and the issuance of a 45% common equity interest in PCA. PCA Holdings LLC, an entity organized and controlled by Madison Dearborn Partners, LLC, acquired the remaining 55% common equity interest in PCA for $236.5 million in cash. These events are collectively referred to as the "Transactions". Because significant veto rights were retained by Pactiv, the carryover basis of accounting was used and no goodwill was recognized.

PCA's consolidated financial statements as of March 31, 2001 and 2000 are unaudited but include all adjustments (consisting only of normal recurring adjustments) that management considers necessary for a fair presentation of such financial statements. These financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and with Article 10 of SEC Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. Operating results during the period ended March 31, 2001 are not necessarily indicative of the results that may be expected for the period ending December 31, 2001.

2. Summary of Accounting Policies

Basis of Consolidation

The accompanying consolidated financial statements of Packaging Corporation of America include all majority-owned subsidiaries. All significant intercompany transactions have been eliminated. The Company has two joint ventures that are carried under the equity method.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts in the financial statements and the accompanying notes. Actual results could differ from those estimates.

Segment Information

PCA is primarily engaged in one line of business: the manufacture and sale of packaging materials, boxes and containers for industrial and consumer markets. No single customer accounts for more than 10% of total revenues. PCA has no foreign operations.

2. Summary of Accounting Policies (Continued)

New Accounting Pronouncements

Effective January 1, 2001, the Company adopted Statement of Financial Accounting Standards ("SFAS") No. 133, "Accounting for Derivative Instruments and Hedging Activities," as amended by SFAS No. 137 and SFAS No. 138. SFAS No. 133 requires the Company to recognize all derivatives as either assets or liabilities and to measure those instruments at fair value. It further provides criteria for derivative instruments to be designated as fair value, cash flow or foreign currency hedges and establishes respective accounting standards for reporting changes in the fair value of the derivative instruments. The Company is required to adjust hedging instruments to fair value in the balance sheet and recognize the offsetting gains or losses as adjustments reported in net income or accumulated other comprehensive income (OCI), as appropriate.

The Company recorded a transition adjustment upon adoption of SFAS No. 133 to recognize its derivative instruments at fair value and to recognize the effective and ineffective portions of the cash flow hedges. The effect of this transition adjustment was to decrease reported net income in the quarter by approximately $0.5 million ($0.8 million pre-tax). The Company also recorded a minimal transition adjustment in OCI and an increase in noncurrent liabilities of approximately $0.8 million.

The Company uses derivative instruments to manage exposures to interest rate risk. The Company's objectives for holding derivatives are to minimize the risks using the most effective methods to eliminate or reduce the impacts of these exposures. The Company has two interest rate collar agreements that protect against rising interest rates and simultaneously guarantee a minimum interest rate. Interest rate collar agreements are accounted for as cash flow hedges.

For the three months ended March 31, 2001, reported net income decreased $0.1 million ($0.1 million pre-tax) for changes in the time value of the interest rate collars, or hedge ineffectiveness. OCI decreased $0.9 million ($1.4 million pre-tax) for hedge effectiveness. Derivative losses included in OCI as of March 31, 2001, will be reclassified into earnings over the lives of the collar agreements, through June 30, 2003.

Revenue Recognition

The Company recognizes revenue as title to the products is transferred to customers.

In the fourth quarter of 2000, the Company adopted EITF 00-10, "Accounting for Shipping and Handling Fees and Costs." Shipping and handling costs are included in cost of sales. Shipping and handling billings to a customer in a sales transaction are included in revenue. Prior year amounts have been reclassed to conform to this treatment.

Comprehensive Income

For the three months ended March 31, 2001, total comprehensive income was $0.9 million less than net income due to derivative losses. There was no difference for the three months ended March 31, 2000.

2. Summary of Accounting Policies (Continued)

Reclassifications

Prior year's financial statements have been reclassified where appropriate to conform with current year presentation.

3. Earnings Per Share

The following table sets forth the computation of basic and diluted income per common share for the periods presented.

(In thousands, except per share data)	Three Months Ended March 31, 2001	Three Months Ended March 31, 2000
Numerator:		
Net income available to common shareholders	$ 27,619	$ 6,609
Denominator:		
Basic common shares outstanding	106,414	101,583
Effect of dilutive securities:		
Stock options	2,545	2,344
Non-vested stock	—	929
Dilutive common shares outstanding	108,959	104,856
Basic income per common share	$ 0.26	$ 0.07
Diluted income per common share	$ 0.25	$ 0.06

4. Inventories

The components of inventories are as follows:

(In thousands)	March 31, 2001	December 31, 2000 (audited)
Raw materials	$ 66,723	$ 71,256
Work in progress	6,083	5,908
Finished goods	54,567	56,157
Supplies and materials	50,823	51,222
Inventories at FIFO cost	178,196	184,543
Excess of FIFO over LIFO cost	(24,937)	(24,831)
Inventory, net	$ 153,259	$ 159,712

An actual valuation of inventory under the LIFO method can be made only at the end of each year based on the inventory levels and costs at that time. Accordingly, interim LIFO calculations must necessarily be based on management's estimates of expected year-end inventory levels and costs. Because these are subject to many forces beyond management's control, interim results are subject to the final year-end LIFO inventory valuation.

Packaging Corporation of America

Notes to Condensed Consolidated Financial Statements (Continued)

(unaudited)

March 31, 2001

5. Summarized Combined Financial Information about Guarantor Subsidiaries

The following is summarized aggregated financial information for Packaging Credit Company, LLC, Dixie Container Corporation and PCA Hydro, Inc., each of which was a wholly-owned subsidiary of PCA and included in the Company's consolidated financial statements. Each of these subsidiaries fully, unconditionally, jointly and severally guaranteed $550.0 million in senior subordinated notes issued by PCA in connection with the Transactions. Separate financial statements of the guarantor subsidiaries are not presented because, in the opinion of management, such financial statements are not material to investors.

(In thousands)	PCA	Guarantor Subs	Non-Guarantor Subs	Eliminations	Total
March 31, 2001					
Current assets	$ 230,990	$ 76,612	$189,637	$ (74,057)	$ 423,182
Non-current assets	1,648,511	65,878	—	(190,748)	1,523,641
Total assets	1,879,501	142,490	189,637	(264,805)	1,946,823
Current liabilities	266,091	7,072	764	(79,595)	194,332
Non-current liabilities	905,683	159	131,000	—	1,036,842
Total liabilities	1,171,774	7,231	131,764	(79,595)	1,231,174
Net assets	$ 707,727	$135,259	$ 57,873	$(185,210)	$ 715,649
December 31, 2000					
Current assets	$ 192,295	$ 63,501	$207,976	$ (60,063)	$ 403,709
Non-current assets	1,663,269	65,883	—	(190,749)	1,538,403
Total assets	1,855,564	129,384	207,976	(250,812)	1,942,112
Current liabilities	278,581	3,441	1,372	(64,846)	218,548
Non-current liabilities	893,978	162	142,000	—	1,036,140
Total liabilities	1,172,559	3,603	143,372	(64,846)	1,254,688
Net assets	$ 683,005	$125,781	$ 64,604	$(185,966)	$ 687,424
Three Months Ended March 31, 2001					
Net sales	$ 454,666	$ —	$ —	$ —	$ 454,666
Pre-tax profit	40,775	13,111	1,970	(9,458)	46,398
Net income	24,116	8,168	1,227	(5,892)	27,619
Three Months Ended March 31, 2000					
Net Sales	$ 475,890	$ —	$ —	$ —	$ 475,890
Pre-tax profit	42,486	13	—	—	42,499
Net income	25,238	8	—	—	25,246

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

Overview

On April 12, 1999, Pactiv Corporation, formerly known as Tenneco Packaging Inc., sold its containerboard and corrugated packaging products business to Packaging Corporation of America for $2.2 billion. We refer to that business in this report as the Group. The $2.2 billion purchase price paid to Pactiv consisted of $246.5 million in cash, the assumption of $1.8 billion of debt incurred by Pactiv immediately prior to the closing, and the issuance of a 45% common equity interest in PCA. PCA Holdings LLC, an entity organized and controlled by Madison Dearborn Partners, LLC, acquired the remaining 55% common equity interest in PCA for $236.5 million in cash. We refer to these events in this report as the Transactions.

PCA's acquisition of the Group as part of the Transactions was accounted for using historical values for the contributed assets. Purchase accounting was not applied because, under the applicable accounting guidance, a change of control was deemed not to have occurred as a result of the participating veto rights held by Pactiv after the closing of the Transactions under the terms of a stockholders agreement.

General

Historically, prices for containerboard have reflected changes in containerboard supply that result from capacity additions and reductions, as well as changes in demand. Containerboard demand is dependent upon both domestic demand for corrugated products and linerboard export activity.

Pulp & Paper Week, an industry publication, in its April 23, 2001 publication, reported that average linerboard and semi-chemical medium prices for 42 lb. Liner-East and 26 lb. Medium-East, which are representative benchmark grades, decreased $5 per ton, or 1%, and $10 per ton, or 2%, respectively, from the previous month. According to Pulp & Paper Week, average prices in April, 2001 for linerboard and corrugating medium were 4% and 10% lower, respectively, than April, 2000 prices.

Results of Operations

Three Months Ended March 31, 2001 Compared to Three Months Ended March 31, 2000

Net Sales

Net sales decreased by $21.2 million, or 4.5%, for the three months ended March 31, 2001 from the comparable period in 2000. The decrease was primarily the result of lower sales volumes of containerboard and corrugated products, partially offset by increased sales prices of corrugated products and containerboard to domestic third parties.

Total corrugated products volume decreased 3.7% for the three months ended March 31, 2001 from the comparable period in 2000.

According to Pulp & Paper Week, average linerboard and semi-chemical medium prices for 42 lb. Liner-East and 26 lb. Medium-East, which are representative benchmark grades, were $460 and $425, respectively, per ton for the three months ended March 31, 2001. This compares to $447 and $427, respectively, per ton for the three months ended March 31, 2000.

Income Before Interest Expense and Taxes

Operating income decreased by $6.8 million, or 9.3%, for the three months ended March 31, 2001 compared to the three months ended March 31, 2000. The decrease in operating income was primarily attributable to the lower sales volumes described above.

Gross margins decreased $1.4 million, or 1.3%, for the three months ended March 31, 2001 from the comparable period in 2000 due to the lower sales volumes described above. Gross margins, as a percent of

net sales, increased to 23.6% in the first quarter of 2001 from 22.8% in the first quarter of 2000 due to increased sales prices of corrugated products and containerboard to domestic third parties.

Selling and administrative expenses increased $1.6 million, or 5.4%, for the three months ended March 31, 2001 compared to the three months ended March 31, 2000. The increase was primarily the result of increased salary and other general selling related expenses.

Corporate overhead for the three months ended March 31, 2001 increased by $0.8 million, or 8.0%, from the comparable period in 2000. The increase was primarily due to increased salary and information technology services expenses.

Interest Expense and Income Taxes

Interest expense decreased by $10.7 million, or 35.3%, for the three months ended March 31, 2001 from the three months ended March 31, 2000, primarily as a result of voluntary prepayments PCA made on its term loans under the senior credit facility.

PCA's effective tax rate was 39.4% for the three months ended March 31, 2001 and 40.6% for the comparable period in 2000. The tax rate is higher than the federal statutory rate of 35% due to state income taxes.

Liquidity and Capital Resources

Cash flow provided by operating activities increased $23.0 million, or 50.8%, for the three months ended March 31, 2001 from the comparable period in 2000. The increase was primarily due to increases in net income and deferred income taxes and a reduction of working capital.

Net cash used for investing activities increased $0.6 million, or 3.0%, for the three months ended March 31, 2001 compared to the three months ended March 31, 2000, primarily as a result of decreased proceeds from asset disposals and increased capital expenditures.

Net cash used for financing activities decreased $2.0 million, or 16.8%, for the three months ended March 31, 2001 from the comparable period in 2000. The decrease was primarily attributable to lower debt prepayments and increased proceeds from the issuance of common stock upon exercise of stock options.

As of March 31, 2001, PCA had commitments for capital expenditures of $62.3 million. PCA's primary sources of liquidity are cash flow from operations and borrowings under PCA's senior revolving credit facility. PCA expects to be able to fund its debt service and capital expenditures, the primary uses of its cash, from these sources.

PCA incurred substantial indebtedness in connection with the Transactions. On April 12, 1999, PCA had approximately $1.8 billion of indebtedness as a result of the debt assumed in connection with completion of the Transactions. As of March 31, 2001, PCA's level of indebtedness had been reduced to approximately $858.0 million through prepayments of its bank debt.

Concurrently with the Transactions, PCA issued 9⅝% senior subordinated notes and 12⅜% senior exchangeable preferred stock and entered into a senior credit facility. The senior credit facility provided for three term loans in an aggregate amount of $1.2 billion and a revolving credit facility with up to $250.0 million in availability. Upon the closing of the Transactions, PCA borrowed the full amount under the term loans. Effective December 14, 1999, PCA elected to reduce its availability under the senior revolving credit facility from $250.0 million to $150.0 million.

In October and November 1999, PCA completed the sales of approximately 405,000 acres of timberland. Total proceeds received from the sales were $263.3 million, resulting in a pre-tax gain of $12.2 million.

On January 28, 2000, PCA became a publicly traded company with an initial public offering of its common stock. On March 3, 2000, PCA used the net proceeds from the offering to redeem all of its outstanding shares of 12⅜% senior exchangeable preferred stock due 2010.

On June 29, 2000, PCA completed the refinancing of its $885.0 million senior credit facility. The refinanced senior credit facility provided for two term loans in an aggregate amount of $735.0 million and a senior revolving credit facility with up to $150.0 million in availability.

On November 16, 2000, PCA completed the sale of approximately 385,000 acres of timberland to Southern Timber Venture, LLC. The Company received $247.9 million in cash and a 33⅓% equity ownership interest in Southern Timber Venture, LLC. PCA recorded a pre-tax gain of $60.4 million, and a portion of the gain was not recognized as a result of PCA's continuing ownership interest.

On November 29, 2000, PCA entered into a three-year, $150.0 million revolving credit facility in connection with the securitization of trade receivables. The facility is secured by PCA's receivables and bears interest at a floating rate based upon commercial paper plus an allowed margin under the agreement. Proceeds received of $142.0 million were used to repay the term loans under the senior credit facility.

The following table provides the weighted average interest rate as of March 31, 2001 for each of the term loans and the revolving credit facility:

Borrowing Arrangement	Weighted Average Interest Rate
Term Loan A	6.63%
Term Loan B	7.10%
Senior Revolving Credit Facility:	
Revolver—Eurodollar	N/A
Revolver—Base Rate	N/A
Three-year Revolving Credit Facility	5.39%

The borrowings under the senior revolving credit facility are available to fund PCA's working capital requirements, capital expenditures and other general corporate purposes. The Term Loan A must be repaid in quarterly installments from December 2002 through June 2006. The Term Loan B must be repaid in quarterly installments from December 2002 through June 2007. The senior revolving credit facility will terminate in 2006. The three-year revolving credit facility will terminate in 2003. As of March 31, 2001, PCA had $150.0 million in availability and no borrowings outstanding under the senior revolving credit facility, and $150.0 million in availability and $131.0 million outstanding under the three-year revolving credit facility.

Since April 12, 1999, PCA has made debt prepayments totalling approximately $911.0 million, using free cash from operations of $400.0 million and proceeds from the sales of timberland of $511.0 million to reduce its borrowings under the term loans and the three-year revolving credit facility.

The instruments governing PCA's indebtedness, including the senior credit facility and the indenture governing the notes, contain financial and other covenants that restrict, among other things, the ability of PCA and its subsidiaries to:

- incur additional indebtedness,
- pay dividends or make certain other restricted payments,
- consummate certain asset sales,
- incur liens,

- enter into certain transactions with affiliates, or
- merge or consolidate with any other person or sell or otherwise dispose of all or substantially all of the assets of PCA.

PCA believes that cash generated from operations will be adequate to meet its anticipated debt service requirements, capital expenditures and working capital needs for the next 12 months, and that cash generated from operations and amounts available under the senior revolving credit facility will be adequate to meet its anticipated debt service requirements, capital expenditures and working capital needs for the foreseeable future. There can be no assurance, however, that PCA's business will generate sufficient cash flow from operations or that future borrowings will be available under the senior credit facility or otherwise to enable it to service its indebtedness, including the senior credit facility, and the notes, to retire the notes when required or to make anticipated capital expenditures. PCA's future operating performance and its ability to service or refinance the notes, to service, extend or refinance the senior credit facility and to pay cash dividends, will be subject to future economic conditions and to financial, business and other factors, many of which are beyond PCA's control.

Market Risk and Risk Management Policies

Historically, the Group has not had any material market risk due to the fact that its debt financing and risk management activities were conducted by Pactiv or Tenneco. As a result of the Transactions, PCA is exposed to the impact of interest rate changes and changes in the market value of its financial instruments. PCA periodically enters into derivatives in order to minimize these risks, but not for trading purposes.

Under the terms of the senior credit agreement dated as of April 12, 1999, PCA was required to maintain for at least two years after the closing of the transactions interest rate protection agreements establishing a fixed maximum interest rate with respect to at least 50% of the outstanding term loans under the senior credit agreement. Upon the refinancing of the senior credit agreement on June 29, 2000, this requirement was deleted.

PCA currently has interest rate collar agreements that protect against rising interest rates and simultaneously guarantee a minimum interest rate. The original notional amount of these collar agreements was $720.0 million. As PCA has made debt prepayments, the need for these collar agreements has diminished. Accordingly, PCA has reduced the notional amount of its collars to $250.0 million as of March 31, 2001. The weighted average floor of the interest rate collar agreements is 5.00% and the weighted average ceiling of the interest rate collar agreements is 6.83%. The interest rate on approximately 81% of PCA's variable-rate debt as of March 31, 2001 is capped. PCA receives payments under the collar agreements if the applicable interest rate (LIBOR or commercial paper) exceeds the ceiling. Correspondingly, PCA makes payments under the collar agreements if the applicable interest rate drops below the floor. In both cases, the amounts received or paid are based upon the notional amount and the difference between the actual interest rate and the ceiling or floor rate. The weighted average duration of the interest rate collar agreements is approximately two years.

PCA's earnings are affected by changes in short-term interest rates as a result of borrowings under its variable-rate debt instruments. If interest rates (LIBOR or commercial paper) for these borrowings increase one percent, PCA's interest expense would increase, and income before income taxes would decrease, by approximately $3.1 million annually, until the applicable interest rate exceeds the ceiling rate. At that point, only 19% of the variable-rate debt as of March 31, 2001, would result in additional interest expense. As of March 31, 2001, the weighted average LIBOR rate was 5.12% and the weighted average commercial paper rate was 5.04%. The effect of an interest rate change to the fair market value of the outstanding debt is insignificant. This analysis does not consider any other impact on fair value that could exist in such an interest rate environment. In the event of a change in interest rates, management could take actions to further mitigate its exposure to the change. However, due to the uncertainty of the specific

actions that would be taken and their possible effects, the sensitivity analysis assumes no changes in PCA's financial structure.

Environmental Matters

PCA is subject to, and must comply with, a variety of federal, state and local environmental laws, particularly those relating to air and water quality, waste disposal and the cleanup of contaminated soil and groundwater. Because environmental regulations are constantly evolving, PCA has incurred, and will continue to incur, costs to maintain compliance with those laws. In particular, the United States Environmental Protection Agency recently finalized the Cluster Rules, which govern pulp and paper mill operations, including those at the Counce, Filer City, Valdosta and Tomahawk mills. Over the next several years, the Cluster Rules will affect PCA's allowable discharges of air and water pollutants, and require PCA to spend money to ensure compliance with those new rules.

As is the case with any industrial operation, PCA has, in the past, incurred costs associated with the remediation of soil or groundwater contamination, as required by the federal Comprehensive Environmental Response, Compensation and Liability Act, commonly known as the federal "Superfund" law, and analogous state laws. Cleanup requirements arise with respect to properties PCA currently owns or operates, former facilities and off-site facilities where PCA has disposed of hazardous substances. Because liability under these laws is strict, meaning that liability is imposed without fault, joint and several, meaning that liability is imposed on each party without regard to contribution, and retroactive, PCA could receive notifications of cleanup liability in the future and this liability could be material. Under the terms of the contribution agreement entered into in connection with the Transactions, Pactiv agreed to retain all liability for all former facilities and all sites associated with pre-closing off-site waste disposal. Pactiv also retained environmentally impaired real property in Filer City, Michigan unrelated to current mill operations.

Impact of Inflation

PCA does not believe that inflation has had a material impact on its financial position or results of operations during the past three years.

Forward-Looking Statements

Certain statements in this Quarterly Report on Form 10-Q are forward-looking statements. Forward-looking statements include statements about our future financial condition, our industry and our business strategy. Statements that contain words such as "anticipate", "believe", "expect", "intend", "estimate", "hope" or similar expressions, are forward-looking statements. These forward-looking statements are based on the current expectations of PCA. Because forward-looking statements involve inherent risks and uncertainties, the plans, actions and actual results of PCA could differ materially. Among the factors that could cause plans, actions and results to differ materially from PCA's current expectations are those identified under the caption "Risk Factors" in PCA's Registration Statements on Form S-4 and Form S-1, each filed with the Securities and Exchange Commission and available at the SEC's website at "www.sec.gov".

Item 3. Quantitative and Qualitative Disclosures about Market Risk.

For a discussion of market risks related to PCA, see Part I, Item 2, "Management's Discussion and Analysis of Financial Condition and Results of Operations—Market Risk and Risk Management Policies" in this Quarterly Report on Form 10-Q.

PART II
OTHER INFORMATION

Item 1. Legal Proceedings.

On May 14, 1999, PCA was named as a defendant in a Consolidated Class Action Complaint which alleged a civil violation of Section 1 of the Sherman Act. The suit, captioned *Winoff Industries, Inc. v. Stone Container Corporation*, MDL No. 1261 (E.D. Pa.), names PCA as a defendant based solely on the allegation that PCA is a successor to the interests of Tenneco Packaging Inc. and Tenneco Inc., both of which were also named as defendants in the suit, along with nine other linerboard manufacturers. The complaint alleges that the defendants, during the period from October 1, 1993 through November 30, 1995, conspired to limit the supply of linerboard, and that the purpose and effect of the alleged conspiracy was artificially to increase prices of corrugated containers. The plaintiffs have moved to certify a class of all persons in the United States who purchased corrugated containers directly from any defendant during the above period, and seek treble damages and attorneys' fees on behalf of the purported class. The Court has yet to rule on the plaintiffs' motion for class certification, and the case is currently set for trial in June, 2002. PCA believes that the plaintiffs' allegations have no merit and intend to defend against the suit vigorously. PCA does not believe that the outcome of this litigation should have a material adverse effect on its financial position, results of operations, or cash flow.

PCA is also party to various legal actions arising in the ordinary course of its business. These legal actions cover a broad variety of claims spanning its entire business. PCA believes that the resolution of these legal actions will not, individually or in the aggregate, have a material adverse effect on its financial condition or results of operations.

Item 2. Changes in Securities and Use of Proceeds.

None.

Item 3. Defaults Upon Senior Securities.

None.

Item 4. Submission of Matters to a Vote of Security Holders.

None.

Item 5. Other Information.

None.

Item 6. Exhibits and Reports on Form 8-K.

(a) The following exhibits are included in this Quarterly Report on Form 10-Q:

None.

(b) Reports on Form 8-K:

None.

SIGNATURE

Pursuant to the requirements 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.

PACKAGING CORPORATION OF AMERICA
(Registrant)

By: /s/ RICHARD B. WEST

Richard B. West
Chief Financial Officer, Vice President and Corporate Secretary (Principal Financial Officer and Authorized Officer)

Date: May 15, 2001