

GEORGIA PACIFIC CORP  
Form 10-Q  
July 29, 2004

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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

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FORM 10-Q

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(Mark One)

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

For the quarterly period ended July 3, 2004

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_  
**Commission File Number 1-3506**

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GEORGIA-PACIFIC CORPORATION

(Exact name of registrant as specified in its charter)

Georgia  
(State or other jurisdiction of  
incorporation or organization)

93-0432081  
(I.R.S. Employer  
Identification Number)

133 Peachtree Street, N.E.,  
Atlanta, Georgia 30303

(Address of Principal Executive Offices) (Zip Code)

Registrant's telephone number, including area code: (404) 652-4000

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Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section

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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

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Act). Yes

No

As of the close of business on July 26, 2004, Georgia-Pacific Corporation had 258,174,072 shares of Georgia-Pacific Common Stock outstanding.

PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

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

	Second Quarter		First Six Months	
	2004	2003	2004	2003
(In millions, except per share amounts)				
Net sales	\$ 5,188	\$ 4,883	\$10,410	\$ 9,321
Costs and expenses:				
Cost of sales	3,893	3,847	7,858	7,368
Selling and distribution	304	321	662	626
Depreciation, amortization and accretion	236	243	480	486
General and administrative	225	207	444	398
Interest, net	178	202	375	406
Other (income) losses, net	(27)	(16)	(1)	62
Total costs and expenses	4,809	4,804	9,818	9,346

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Income (loss) from continuing operations before income taxes	379	79	592	(25)
Provision (benefit) for income taxes	149	25	220	(28)

Income from continuing operations	230	54	372	3
(Loss) income from discontinued operations, net of taxes	(10)	7	(5)	--

Income before accounting change	220	61	367	3
Cumulative effect of accounting change, net of taxes	--	--	--	28

Net income	\$ 220	\$ 61	\$ 367	\$ 31
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Basic per share:	\$ 0.90	\$ 0.22	\$ 1.46	\$ 0.01
	(0.04)	0.02	(0.02)	--

Income from continuing operations				
(Loss) income from discontinued operations, net of taxes				

Income before accounting change	\$ 0.86	\$ 0.24	\$ 1.44	\$ 0.01
Cumulative effect of accounting change, net of taxes	--	--	--	0.11

Net income	\$ 0.86	\$ 0.24	\$ 1.44	\$ 0.12
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Diluted per share:	\$ 0.88	\$ 0.22	\$ 1.42	\$ 0.01
	(0.04)	0.02	(0.02)	--

Income from continuing operations				
(Loss) income from discontinued operations, net of taxes				

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Income before accounting change	\$ 0.84	\$ 0.24	\$1.40	\$ 0.01
Cumulative effect of accounting change, net of taxes	--	--	--	0.11
<b>Net income</b>				
	\$ 0.84	\$ 0.24	\$ 1.40	\$ 0.12
<b>Shares (denominator):</b>				
Weighted average shares outstanding	255.1	250.1	254.3	250.1
<b>Dilutive securities:</b>				
Options and restricted stock	7.5	0.6	7.5	0.4
<b>Total assuming conversion</b>				
	262.6	250.7	261.8	250.5

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

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

(In millions, except per share amount)	First Six Months	
	2004	2003
Cash flows from operating activities	\$ 367	\$ 31
Net income		
Adjustments to reconcile net income to cash provided by operations (excluding the effect of dispositions):	--	(28)
Cumulative effect of accounting changes, net of taxes	(3)	63
Other (income) loss, net	493	522
Depreciation, amortization and accretion	(22)	(107)
Deferred income taxes	(497)	(272)
Increase in receivables	(68)	(23)
Increase in inventories	223	48
Increase in accounts payable	37	22
Change in other working capital	92	340
	(149)	42

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Change in taxes payable/receivable	4	30
Change in other assets and other long-term liabilities		
Other		
<b>Cash provided by operations</b>	<b>477</b>	<b>668</b>
<b>Cash flows from investing activities</b>		
	(288)	(310)
	(23)	--
Property, plant and equipment investments	1,386	17
Acquisitions	(34)	(19)
Net proceeds from sales of assets		
Other		
<b>Cash provided by (used for) investing activities</b>	<b>1,041</b>	<b>(312)</b>
<b>Cash flows from financing activities</b>		
	(4,412)	(4,800)
	3,266	4,441
Repayments of long-term debt	(13)	(47)
Additions to long-term debt	(35)	--
Fees paid to issue debt	(60)	(54)
Fees paid to retire debt	(181)	190
Net decrease in bank overdrafts	49	--
Net increase (decrease) in short-term debt	(64)	(63)
Proceeds from option plan exercises		
Cash dividends paid (\$0.25 per share)		
<b>Cash used for financing activities</b>	<b>(1,450)</b>	<b>(333)</b>
Increase in cash	68	23
Balance at beginning of period	51	42
<b>Balance at end of period</b>	<b>\$ 119</b>	<b>\$ 65</b>

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

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

(In millions, except shares and per share amounts)	July 3, 2004	January 3, 2004
<b>ASSETS</b>		
Current assets		
Cash and equivalents	\$ 119	\$ 51
Receivables, less allowances of \$32 and \$36, respectively	1,906	1,542
Inventories	1,799	1,848
Deferred income tax assets	125	117
Current net assets held for sale	--	739

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Other current assets	332	301
<b>Total current assets</b>	<b>4,281</b>	<b>4,598</b>
Property, plant and equipment		
Land, buildings, machinery and equipment, at cost	17,898	17,758
Accumulated depreciation	(9,548)	(9,176)
<b>Property, plant and equipment, net</b>	<b>8,350</b>	<b>8,582</b>
<b>Goodwill, net</b>	<b>7,461</b>	<b>7,484</b>
<b>Intangible assets, net</b>	<b>693</b>	<b>716</b>
<b>Net assets held for sale</b>	<b>--</b>	<b>757</b>
<b>Other assets</b>	<b>2,238</b>	<b>2,268</b>
<b>Total assets</b>	<b>\$ 23,023</b>	<b>\$ 24,405</b>

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

(In millions, except shares and per share amounts)	July 3, 2004	January 3, 2004
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
<b>Current liabilities</b>		
Secured borrowings and other short-term notes	\$ 508	\$ 689
Current portion of long-term debt	395	789
Accounts payable	1,465	1,404
Accrued compensation	241	244
Current net liabilities held for sale	--	189
Other current liabilities	1,239	1,107
<b>Total current liabilities</b>	<b>3,848</b>	<b>4,422</b>
<b>Long-term debt, excluding current portion</b>	<b>8,334</b>	<b>9,074</b>
<b>Net liabilities held for sale</b>	<b>--</b>	<b>206</b>
<b>Other long-term liabilities</b>	<b>3,605</b>	<b>3,826</b>
<b>Deferred income tax liabilities</b>	<b>1,487</b>	<b>1,483</b>

Commitments and contingencies (

Note 12)

Shareholders' equity		
Preferred stock, no par value; 10,000,000 shares authorized; no shares issued or outstanding	--	--
Junior preferred stock, no par value; 25,000,000 shares authorized; no shares issued or outstanding	--	--
Common stock, par value \$0.80; 400,000,000 shares authorized; 256,171,000 and 252,980,000 shares issued and outstanding	205	202
Additional paid-in capital	3,561	3,473
Retained earnings	1,899	1,596
Long-term incentive plan deferred compensation	(1)	(1)
Accumulated other comprehensive loss	85	124
<b>Total shareholders' equity</b>	<b>5,749</b>	<b>5,394</b>
<b>Total liabilities and shareholders' equity</b>	<b>\$ 23,023</b>	<b>\$ 24,405</b>

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

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

(In millions)	Second Quarter		First Six Months	
	2004	2003	2004	2003
Net income	\$ 220	\$ 61	\$ 367	\$ 31
Other comprehensive income (loss), net of tax:				
Foreign currency translation adjustments	(21)	67	(65)	124
Derivative instruments:				
Fair market value adjustments on derivatives	--	(2)	--	(3)
Reclassification adjustments for losses included in net income	--	4	--	7
Unrealized gain on securities	26	--	26	--
Minimum pension liability adjustment				
<b>Comprehensive income</b>	<b>\$ 225</b>	<b>\$ 130</b>	<b>\$ 328</b>	<b>\$ 163</b>

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

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)  
GEORGIA-PACIFIC CORPORATION  
July 3, 2004

1. **PRINCIPLES OF PRESENTATION AND ACCOUNTING POLICIES.** These consolidated financial statements include the accounts of Georgia-Pacific Corporation and subsidiaries. We prepared the consolidated financial statements following the requirements of the Securities and Exchange Commission (SEC) for interim reporting. As permitted under those rules, certain footnotes or other financial information that are normally required by GAAP (accounting principles generally accepted in the United States of America) can be condensed or omitted. All significant intercompany balances and transactions were eliminated in consolidation.

We are responsible for the unaudited financial statements included in this document. The financial statements include all normal and recurring adjustments that are considered necessary for the fair presentation of our financial position, results of operations and cash flows. These consolidated financial statements should be read in conjunction with the consolidated financial statements and notes included in our audited financial statements for the fiscal year ended January 3, 2004 in our

Form 8-K filed with the SEC on May 20, 2004 reflecting our non-integrated pulp businesses as discontinued operations.

Certain 2003 amounts have been reclassified to conform with the 2004 presentation.

On May 7, 2004, we completed the sale of our non-integrated mills at Brunswick, Georgia, and New Augusta, Mississippi, as well as affiliated assets, to Koch Cellulose, LLC ("Koch") and its subsidiaries. These pulp businesses were reported as discontinued operations through the date of the sale and the related assets and liabilities were classified as held for sale effective February 26, 2004 (the date of the definitive agreement). Accordingly, we ceased depreciation of the related assets on February 26, 2004. These pulp businesses were previously reported in the bleached pulp and paper segment.

We classify certain shipping and handling costs as selling and distribution expenses. Shipping and handling costs included in selling and distribution expenses were \$79 million and \$182 million for the second quarter and first six months of 2004, respectively, and \$100 million and \$195 million for the second quarter and first six months of 2003, respectively.

Other (income) losses, net



The following amounts are included in Other (income) losses, net

(In millions)	Second Quarter		First Six Months	
	2004	2003	2004	2003
Asset impairments:				
Bellingham	\$ 11	\$ --	\$ 11	\$ --
Old Town	--	--	--	74
Other	2	3	2	7
Early extinguishment of debt	27	--	53	--
Gain on asset sales, retirements and disposals, net	(65)	(17)	(65)	(17)
Other	(2)	(2)	(2)	(2)
Other (income) losses, net	\$ (27)	\$ (16)	\$ (1)	\$ 62

### Stock-Based Compensation

Effective December 29, 2002, we adopted Statement of Financial Accounting Standards ("SFAS") No. 148, *Accounting for Stock-Based Compensation--Transition and Disclosure* ("SFAS No. 148"), an amendment of SFAS No. 123, *Accounting for Stock-Based Compensation* ("SFAS No. 123"). SFAS No. 148 provides alternative methods of transition to SFAS No. 123's fair value method of accounting for stock-based compensation and amends the disclosure provisions of SFAS No. 123. We utilized the prospective method in accordance with SFAS No. 148 and applied the expense recognition provisions of SFAS No. 123 to stock options awarded or modified in 2003 and thereafter. Prior to 2003, we accounted for our stock-based compensation plans under APB Opinion No. 25, *Accounting for Stock Issued to Employees* ("APB No. 25"), and disclosed pro forma effects of the plans on net income and earnings per share as provided under SFAS No. 123. Because the fair market value on the date of grant was equal to the exercise price, no compensation expense had been recognized under APB No. 25 for stock options issued prior to 2003. Had compensation cost for the options issued prior to 2003 been determined based on the fair value at the grant dates consistent with the method of SFAS No. 123, the pro forma net income and earnings per share would have been as follows:

Second Quarter

First Six Months

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(In millions, except per share amounts)	2004	2003	2004	2003
Net income as reported	\$ 220	\$ 61	\$ 367	\$ 31
Less total stock-based employee compensation expense determined under the fair value based method, net of taxes	(1)	(2)	(2)	(4)
Pro forma net income	219	59	365	27
Stock based employee compensation cost, net of taxes, included in the determination of net income as reported	23	4	46	6
Basic net income per share:				
As reported	0.86	0.24	1.44	0.12
Pro forma	0.86	0.23	1.44	0.10
Diluted net income per share:				
As reported	0.84	0.24	1.40	0.12
Pro forma	0.84	0.23	1.40	0.10

Accounting Changes

In January 2003, the Financial Accounting Standards Board (the "FASB") released Interpretation No. 46, *Consolidation of Variable Interest Entities* ("FIN 46"). FIN 46 requires that all primary beneficiaries of Variable Interest Entities (VIE) consolidate that entity in their financial statements. FIN 46 is effective immediately for VIEs created after January 31, 2003 and for VIEs in which an enterprise obtains an interest after that date. It applies in the first fiscal year or interim period beginning after June 15, 2003, to VIEs in which an enterprise holds a variable interest it acquired before February 1, 2003. In December 2003, the FASB published a revision to FIN 46 ("FIN 46R") to clarify some of the provisions of the interpretation and defer the effective date of implementation for certain entities. Under the guidance of FIN 46R, entities that do not have interests in structures that are commonly referred to as special purpose entities are required to apply the provisions of the interpretation in financials statements for periods ending after March 14, 2004. We do not have interests in special purpose entities that are not consolidated.

During the second quarter of 2004, we adopted FASB Staff Position ("FSP") FAS 106-2 ("the FSP"), *Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003*. The FSP provides specific guidance on how to account for the subsidy provided by the Medicare Prescription Drug, Improvement and Modernization Act of 2003 ("the Act"). The FSP provides for either retroactive application to the date of enactment or prospective application from the date

of adoption. We have elected retroactive application to the date of enactment, the impact of which was a reduction to net postretirement benefit cost of approximately \$2 million in the second quarter of 2004 and a reduction of the accumulated postretirement benefit obligation of approximately \$67 million.

2. **PROVISION FOR INCOME TAXES.** The effective tax rate in 2004 was higher than the statutory rate primarily because of state taxes and taxes related to the sale of our interest in a Brazilian pulp business, partially offset by lower international income tax rates. The effective tax rate in 2003 was lower than the statutory rate primarily because of lower international income tax rates, utilization of state tax credits and the first quarter reversal of approximately \$10 million of income tax contingency reserves no longer required in Europe.
3. **EARNINGS PER SHARE.** Basic earnings per share is computed based on net income and the weighted average number of common shares outstanding. Diluted earnings per share reflect the assumed issuance of common shares under long-term incentive stock option and stock purchase plans. The increase in dilutive securities during 2004 was due primarily to an increase in the number of shares potentially issuable under our performance awards. The computation of diluted earnings per share does not assume conversion or exercise of securities that would have an antidilutive effect on earnings per share.
4. **SUPPLEMENTAL DISCLOSURES -- CONSOLIDATED STATEMENTS OF CASH FLOWS.** The cash impact of interest and income taxes is reflected in the table below. The effect of foreign currency exchange rate changes on cash was not material in either period.

(In millions)	First six months	
	2004	2003
Total interest costs	\$ 384	\$ 408
Interest capitalized	(9)	(2)
Interest expense	\$ 375	\$ 406
Interest paid	\$ 399	\$ 342
Income tax paid (refunds received), net	\$ 198	\$ (265)
Debt assumed by buyer	\$ 73	\$ --

Interest expense allocated to discontinued operations was \$5 and \$7 million for the first six months of 2004 and 2003, respectively.

5. **DIVESTITURES.**

Building Products Distribution

On May 7, 2004, we completed the sale of our building products distribution segment to a new company owned by Cerberus Capital Management L.P., a private investment firm, and members of the building products distribution business' management team, for \$767 million in cash and a receivable of approximately \$38 million, subject to working capital adjustments. In addition, we received \$173 million in cash in June to settle an intercompany payable related to product sold to the building products distribution business prior to closing. This transaction resulted in a pre-tax gain of \$7 million (\$4 million after-tax gain) and was included in "Other (income) losses, net" on the statements of operations. The working capital adjustment has not been finalized.

In addition, we entered into a six-year agreement for the building products distribution business to continue purchasing structural panels, lumber and other building products manufactured by us. This supply agreement contains substantially similar terms as the previous arrangement between our building products manufacturing and building products distribution businesses. Because our continuing involvement with this business via this supply agreement is considered significant, the building products distribution business is not permitted to be reported as a discontinued operation in accordance with Statement of Financial Accounting Standards ("SFAS") No. 144, *"Accounting for the Impairment and Disposal of Long-Lived*

Assets."

The building products distribution business was deemed to be held for sale and the related assets and liabilities classified as such effective March 12, 2004 (the date of the definitive agreement). Accordingly, we ceased depreciation of the related assets on that date .

The following are major classes of assets and liabilities for the building products distribution business that were held for sale at January 3, 2004:

**BUILDING PRODUCTS DISTRIBUTION ASSETS AND LIABILITIES HELD FOR SALE  
CONDENSED BALANCE SHEETS  
(Unaudited)**

(In millions)

<b>ASSETS</b>	
Current assets	\$ 571
Property, plant and equipment, net	201
<b>Total assets</b>	<b>\$ 772</b>
<b>LIABILITIES:</b>	
Current liabilities	\$ 126
Deferred income tax liabilities	3
<b>Total liabilities</b>	<b>\$ 129</b>

Net assets	\$ 643
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#### Non-integrated Pulp Mills

On May 7, 2004, we completed the sale of our non-integrated mills at Brunswick, Georgia, and New Augusta, Mississippi, along with a short-line railroad, to Koch Cellulose, LLC ("Koch") and its subsidiaries for \$511 million in cash and a receivable of approximately \$9 million for working capital. In addition, Koch assumed \$73 million of indebtedness. This transaction resulted in a pre-tax gain of \$2 million and an after tax loss of \$15 million that was included in discontinued operations on the statements of operations. The working capital adjustment has not been finalized.

These pulp businesses were reported as discontinued operations through the date of the sale and the related assets and liabilities were classified as held for sale effective February 26, 2004 (the date of the definitive agreement). Accordingly, we ceased depreciation of the related assets on February 26, 2004. These pulp businesses were previously reported in the bleached pulp and paper segment.

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The following are major classes of assets and liabilities for these discontinued operations that were held for sale at January 3, 2004:

#### DISCONTINUED OPERATIONS CONDENSED BALANCE SHEETS (Unaudited)

(In millions)

<b>ASSETS</b>	
Current assets	\$ 168
Property, plant and equipment, net	338
Goodwill, net	172
Other assets	1
<b>Total assets</b>	<b>\$ 679</b>
<b>LIABILITIES:</b>	
Current liabilities	\$ 63
Long-term debt	97
Deferred income tax liabilities	100
Other long-term liabilities	6
<b>Total liabilities</b>	<b>\$ 266</b>
<b>Net assets</b>	<b>\$ 413</b>

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Operating results of these discontinued operations are shown below:

DISCONTINUED OPERATIONS  
CONDENSED STATEMENTS OF OPERATIONS  
(Unaudited)

(In millions)	Second Quarter		First Six Months	
	2004	2003	2004	2003
Net sales	\$ 63	\$ 165	\$ 220	\$ 294
Costs and expenses:				
Cost of sales	51	126	178	239
Selling and distribution	2	4	6	8
Depreciation, amortization and accretion	--	18	13	36
General and administrative	1	3	4	6
Interest, net	2	4	5	7
Other income, net	(2)	--	(2)	--
Total costs and expenses	54	155	204	296
Income (loss) from discontinuing operations before income taxes	9	10	16	(2)
Provision (benefit) for income taxes	19	3	21	(2)
(Loss) income from discontinued operations, net of taxes	\$ (10)	\$ 7	\$ (5)	\$ --

The interest expense allocated to the discontinued operations represents the interest associated with the debt that was assumed by the buyer and interest on debt that was required to be repaid as a result of the disposal transaction.

#### Other Asset Sales

During the second quarter of 2004, we sold all of our interests in a Brazilian pulp business for \$71 million in cash and a receivable of \$4 million. This transaction resulted in a pre-tax gain of \$26 million (\$8 million after-tax gain) and was included in "Other (income) losses, net" on the statements of operations.

During the second quarter of 2004, we sold certain packaging assets and an aircraft and recognized a pre-tax gain of \$26 million (\$16 million after-tax gain) which was included in "Other (income) losses, net" on the statements of operations.

6. **ASSET IMPAIRMENT AND RESTRUCTURING.** In June 2004, we signed a letter of intent with the Bellingham Port Authority (the "Port") to sell our Bellingham facilities to the Port and lease back certain of those facilities. The Port will assume our responsibility for all environmental liabilities associated with the facility. In connection with this agreement, we determined that the value of the related assets were impaired. Accordingly, in the second quarter of 2004, we recorded pre-tax charges to earnings of \$11 million for asset impairments. Assuming the parties reach a formal agreement for this transaction, we expect closing to occur in the fourth quarter of 2004.

On April 4, 2003, we announced that we would close tissue-manufacturing and converting operations at our Old Town, Maine mill. The mill's pulp and dryer operations are continuing to operate. The determination to close the tissue operations was based on excess capacity of tissue production, the mill's geographic location and high energy and fiber costs. In connection with this closure, we determined that the value of related tissue assets and certain pulp assets at this location was impaired. Accordingly, in the first quarter of 2003, we recorded a pre-tax impairment charge to earnings in the North America consumer products segment and bleached pulp and paper segment of \$25 million and \$49 million, respectively. In the second quarter of 2003, we recorded a pre-tax charge of \$7 million and \$4 million in the North American consumer products segment for related severance and business exit costs, respectively. Following the impairment charge, the carrying value of fixed assets was approximately \$75 million. The fair value of the impaired assets was determined using the present value of expected future cash flows. This impairment charge was recorded in "Other losses, net" in the accompanying consolidated statements of operations.

On May 2, 2003, the Governor of Maine announced an economic support plan that enabled us to restart one of our closed tissue machines along with eight converting lines and retain related manufacturing and support personnel. In accordance with generally accepted accounting principles, none of the impairment charge recorded in the first quarter of 2003 was reversed.

In connection with the acquisition of Fort James, we recorded liabilities totaling approximately \$78 million for employee termination costs relating to approximately 960 hourly and salaried employees. In addition, we determined that we would strategically reposition our communication papers business to focus on faster-growing paper segments by retiring four high-cost paper machines and associated pulping facilities at our Camas, Washington mill and recorded liabilities of approximately \$26 million to exit these activities. In addition, we recorded liabilities of \$35 million primarily for lease and contract termination costs at administrative facilities that have been or will be closed in California, Connecticut, Illinois, Virginia, Wisconsin and Europe. During 2002 and 2001,

approximately 779 employees were terminated and approximately \$69 million of the reserve was used to pay termination benefits. During the first six months of 2003, approximately 152 employees were terminated and approximately \$5 million of the reserve was used to pay termination benefits. The remaining employee terminations and Camas closing activities (primarily demolition activities) are expected to be completed by the third quarter of 2004 due to timing of receipt of the requisite permits. The leases and contracts at the administrative facilities expire through 2012. The following table provides a rollforward of these reserves from January 3, 2004 through July 3, 2004:

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Type of Cost (In millions)	Liability Balance at January 3, 2004	Use	Liability Balance at July 3, 2004
Employee termination	\$ 4	\$ --	\$ 4
Facility closing costs	30	(7)	23
<b>Total</b>	<b>\$ 34</b>	<b>\$ (7)</b>	<b>\$ 27</b>

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

(In millions)	July 3, 2004	January 3, 2004
Raw materials	\$ 589	\$ 625
Finished goods	822	832
Supplies	495	489
LIFO reserve	(107)	(98)
<b>Total inventories</b>	<b>\$ 1,799</b>	<b>\$ 1,848</b>

8. GOODWILL AND INTANGIBLE ASSETS. Effective December 30, 2001, we adopted SFAS No. 141, *Business Combinations*, and SFAS No. 142, *Goodwill and Other Intangible Assets*. SFAS No. 141 eliminates the pooling of interests method of accounting for business combinations initiated after June 30, 2001. SFAS No. 142 requires that entities assess the fair value of the net assets underlying all acquisition-related goodwill on a reporting unit basis effective beginning in 2002. When the fair value is less than the related carrying value, entities are required to reduce the amount of goodwill. Our reporting units are: structural panels, lumber, industrial wood products, gypsum, chemical, packaging, pulp, paper, North American retail towel and tissue, North American commercial towel and tissue, Dixie, and international consumer products.

On May 7, 2004, we sold our non-integrated pulp mills at Brunswick, Georgia, and New Augusta, Mississippi, along with a short-line railroad to Koch. The goodwill associated with the pulp mill and



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the railroad was \$169 million and \$3 million, respectively, at January 3, 2004, and was included in net assets held for sale effective February 26, 2004 (the date of the definitive agreement)

The changes in the carrying amount of goodwill for the first six months of 2004 are as follows:

(In millions)	North America Consumer Products	International Consumer Products	Packaging	Building Products Manufacturing	Consolidated
		\$ 987			
Balance as of January 3, 2004	\$ 5,831	--	\$ 630	\$ 36	\$ 7,484
Goodwill acquired during the year	--	--	1	--	1
Reclassifications	2		--	--	2
Foreign currency translation	--	(26)	--	--	(26)
Balance as of July 3, 2004	\$ 5,833	\$ 961	\$ 631	\$ 36	\$ 7,461

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Intangible Assets

The following table sets forth information for intangible assets subject to amortization:

(In millions)	As of July 3, 2004		As of January 3, 2004	
	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Trademarks	\$ 675	\$ 54	\$ 677	\$ 40
Patents and other	137	65	132	53
Total	\$ 812	\$ 119	\$ 809	\$ 93

Aggregate Amortization  
Expense:

\$ 16

First six months of 2004	=====
Estimated Amortization Expense:	\$ 29
For fiscal year 2004	29
For fiscal year 2005	20
For fiscal year 2006	20
For fiscal year 2007	20
For fiscal year 2008	

9. **ASSET RETIREMENT OBLIGATIONS.** Effective December 29, 2002, we changed our method of accounting for asset retirement obligations in accordance with SFAS No. 143. Under SFAS No. 143, we recognize asset retirement obligations in the period in which they are incurred if a reasonable estimate of the fair value can be made. When the liability is initially recorded, we capitalize the cost by increasing the carrying amount of the related long-lived asset. Over time, the liability is accreted to its present value and the capitalized cost is depreciated over the useful life of the related asset. Upon settlement of the liability, we will recognize a gain or loss for any difference between the settlement amount and the liability recorded.

Our asset retirement obligations consist primarily of landfill capping and closure and post-closure costs and quarry reclamation costs. We are legally required to perform capping and closure and post-closure care on the landfills and reclamation on the quarries. In accordance with SFAS No. 143, for each landfill and quarry we recognized the fair value of a liability for an asset retirement obligation and capitalized that cost as part of the cost basis of the related asset. The related assets are being depreciated on a straight-line basis over 25-years. We have additional asset retirement obligations with indeterminate settlement dates; the fair value of these asset retirement obligations cannot be estimated due to the lack of sufficient information to estimate a range of potential settlement dates for the obligation. An asset retirement obligation related to these assets will be recognized when we know such information.

The following table describes changes to our asset retirement obligation liability:

(In millions)	First Six Months	
	2004	2003
Asset retirement obligation at the beginning of the year	\$ 49	\$ 67
Net transition adjustments	--	(21)
Accretion expense	1	2
Payments	(1)	--
Write-offs	(1)	--
Asset retirement obligation at the end of the second quarter	\$ 48	\$ 51

The asset retirement obligation liability balances were as follows:

(In millions)	July 3, 2004	January 3, 2004
Amounts of liability for asset retirement obligations at beginning of period	\$ 49	\$ 46
Amounts of liability for asset retirement obligations at end of period	\$ 48	\$ 49

10. DEBT. Our debt decreased by \$1,411 million to \$9,237 million at July 3, 2004 from \$10,648 million at January 3, 2004. This decrease includes the effect of changes in foreign currency exchange rates of \$17 million during this time period. For the six months ended July 3, 2004, the weighted average interest rate on our total debt, including outstanding interest rate exchange agreements, was 7.2%.

On July 2, 2004, we entered into a new \$2.5 billion, five-year, senior unsecured credit facility ("Senior Credit Facility") that includes a \$500 million non-amortizing term loan. This new credit facility matures July 2, 2009 and replaces a \$2.25 billion, five-year credit facility that would have matured November 3, 2005. In connection with this new facility, we recorded a pre-tax charge of approximately \$3 million to write off certain previously deferred debt issuance costs during the second quarter of 2004.

As of July 3, 2004, we had \$508 million outstanding under our \$700 million accounts receivable secured borrowing program. G-P Receivables, Inc. ("G-P Receivables") is our wholly owned subsidiary and is the special purpose entity into which some of our receivables and the receivables of participating domestic subsidiaries are sold. G-P Receivables, in turn, sells an interest in the receivables to the various banks and entities. This program is accounted for as a secured borrowing. The receivables outstanding under these programs and the corresponding debt are included as "Receivables" and "Secured borrowings and other short-term notes," respectively, in the accompanying balance sheets. As collections reduce previously pledged interests, new receivables may be pledged. G-P Receivables is a separate corporate entity and its assets will be available first and foremost to satisfy the claims of its creditors. We repurchased the receivable interest sold into the program related to the building products distribution segment and the non-integrated pulp business. Those receivables were transferred to the purchasers of those businesses pursuant to the divestitures described in Note 5. The amount of those repurchases was \$416 million and \$12 million, respectively.

On December 11, 2003, we completed a private placement of \$500 million of 8% senior notes, due in 2024. Net proceeds from the private placement were used to pay down a portion of our five-year credit facility that would have matured in November 2005, described above. On July 1, 2004, we completed an offer to exchange these notes for new notes with substantially identical terms that are registered under the Securities Act. We paid approximately \$7 million in fees and expenses associated with this transaction. The fees are being amortized over the term of the senior notes.

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On February 27, 2004, we called \$243 million of our 9.875% debentures due November 1, 2021. On March 31, 2004, we also called \$250 million of our 9.625% debentures due March 15, 2022. In

conjunction with these transactions we recorded a pre-tax charge of \$26 million for call premiums and a write off of deferred debt issuance costs during the first quarter of 2004. This charge for the early extinguishment of debt was included in "Other losses, net" in the accompanying statements of operations.

On April 20, 2004, we called \$250 million of our 9.5% debentures due May 15, 2022. On May 6, 2004, we also called \$240 million of our 9.125% debentures due July 1, 2022. In conjunction with these transactions, we recorded a pre-tax charge of \$24 million for call premiums and to write off deferred debt issuance costs during the second quarter of 2004. This charge for the early extinguishment of debt was included in "Other losses, net" in the accompanying statements of operations.

On April 2, 2004, we borrowed a total of \$400 million of 2.6% short-term notes which were repaid on June 7, 2004. Net proceeds from this borrowing were used to pay down a portion of our five-year credit facility that would have matured in November 2005, described above.

In connection with the sale of our non-integrated pulp mills and short-line railroad to Koch on May 7, 2004 (see Note 5), Koch assumed \$73 million of indebtedness. In addition, we defeased an outstanding \$24 million tax-exempt bond on April 30, 2004 in order to transfer certain assets to Koch.

On July 14, 2004, Moody's Investor Service upgraded our liquidity rating from SGL-3 (adequate) to SGL-2 (good). Moody's indicated that the upgrade was in response to our Senior Credit Facility that we entered into on July 2, 2004.

On May 4, 2004, Standard & Poor's Ratings Services revised its outlook on our long-term debt to 'stable' from 'negative' and affirmed its rating of BB+. Standard & Poor's Ratings Services indicated that the ratings actions reflect our improving financial profile and much better liquidity. On April 28, 2004, Fitch Ratings increased our senior unsecured long-term debt ratings to BB+ from BB and changed our rating outlook to 'stable'. Fitch Ratings indicated that this upgrade is primarily due to debt reductions resulting from expected asset sales as well as increased cash flows from operations. Additionally, on April 14, 2004, Moody's Investor Service revised the outlook for our Senior Implied Ba2 debt rating to 'stable' from 'negative' citing our plans to reduce debt with proceeds from our expected asset sales.

At July 3, 2004, we had \$500 million outstanding under our new Senior Credit Facility at a weighted-average interest rate of 2.9% with a maturity date of July 2, 2009. In addition, \$570 million of borrowing capacity under this facility was committed to support outstanding letters of credit and similar instruments. Amounts outstanding under this facility are included in "Long-term debt, excluding current portion" in the accompanying consolidated balance sheets.

The amounts outstanding under our Senior Credit Facility include the following:

<b>(In millions)</b>	<b>July 3, 2004</b>
Commitments:	\$ 2,000
	500
Revolving Loans	

Term Loans	
Credit facilities available	2,500
Amounts Outstanding:	
	(570)
	(500)
Letters of Credit Agreements*	
Term Loans due July 2009, average rate of 2.9%	
Total credit balance outstanding	(1,070)
Total credit available	\$ 1,430

\* The Letters of Credit Agreements only include Standby Letters of Credit supported by the Senior Credit Facility.

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Covenants in the Senior Credit Facility require a maximum leverage ratio (as defined) of 67.50% for each remaining fiscal quarter during 2004 and 65.00% thereafter, a minimum interest coverage ratio (as defined) of 2.50 to 1.00 in any quarter hereafter, and a minimum net worth (as defined) that is not less than the sum of 80% of consolidated net worth (as defined) as of the end of our fiscal year 2003 and an amount equal to 50% of consolidated net income (as defined) earned in each fiscal quarter commencing on January 4, 2004.

<b>(In millions)</b>	July 3, 2004
Adjusted Net Worth:	
	\$ 5,749
	(85)
Net worth	--
Accumulated other comprehensive income	
Goodwill impairments	
Adjusted Net Worth	5,664
Required Net Worth:	
	4,216
	184
80% of Net Worth as of January 3, 2004	
50% of Net Income beginning first quarter 2004*	

Required Net Worth	4,400
Adjusted Net Worth surplus	\$ 1,264

\* Does not include quarters with net losses.

Our borrowing arrangements contain a number of financial and non-financial covenants, which restrict our activities. We were in compliance with these debt covenants as of July 3, 2004, with a leverage ratio of 61.99%, an interest coverage ratio of 3.43 to 1.00, and an adjusted net worth surplus (as defined) as shown above. In addition, certain agreements contain cross-default provisions. Our continued compliance with these restrictive covenants is dependent on a number of factors, many of which are outside of our control. Should events occur that result in noncompliance, we believe there are remedies available that are acceptable to our lenders and us.

Approximately \$80 million of our revenue bonds are supported by letters of credit that expire within one year. We intend to renew the letters of credit supporting these revenue bonds. Therefore, maturities of these obligations are reflected in accordance with their stated terms.

At July 3, 2004, we had interest rate exchange agreements (a collar) that effectively capped \$47 million of floating rate obligations to a maximum interest rate of 7.5% and established a minimum interest rate on these obligations of 5.5%. Our interest expense is unaffected by these agreements when the market interest rate falls within this range. For the six months ended July 3, 2004, these agreements reduced interest expense by less than \$1 million. The agreements had a weighted-average maturity of approximately one year at July 3, 2004.

The estimated fair value of our interest rate exchange agreements at July 3, 2004 was a \$2 million asset. The asset balance represents the estimated amount we would have received if these agreements were terminated on July 3, 2004. The fair value at July 3, 2004 was estimated by calculating the present value of anticipated cash flows. The discount rate used was an estimated borrowing rate for similar debt instruments with like maturities.

At July 3, 2004 we had \$1,165 million of floating rate debt outstanding, which represented approximately 13% of our total debt balance.

As of July 3, 2004, we had \$1.5 billion of debt and equity securities available for issuance under a shelf registration statement filed with the Securities and Exchange Commission in 2000.

## 11. RETIREMENT PLANS

### Defined Benefit Pension Plans

Most of our employees participate in noncontributory defined benefit pension plans. These include plans that are administered solely by us and union-administered multiemployer plans. Our funding policy for solely administered plans is based on actuarial calculations and the applicable requirements of federal law. Contributions to multiemployer plans are generally based on negotiated labor contracts.

Benefits under the majority of plans for hourly employees (including multiemployer plans) are primarily related to years of service. We have separate plans for salaried employees and officers under which benefits are primarily related to compensation and age. The officers' plan and the supplemental retirement plan for eligible executives are not funded and are nonqualified for federal income tax purposes.

Net periodic pension cost for our pension plans during the second quarters and first six months of 2004 and 2003 included the following components:

(In millions)	Second Quarter		First Six Months	
	2004	2003	2004	2003
Service cost of benefits earned	\$ 37	\$ 35	\$ 74	\$ 69
Interest cost on projected benefit obligation	63	61	126	123
Expected return on plan assets	(72)	(61)	(144)	(121)
Amortization of losses	9	12	17	24
Amortization of prior service cost	4	6	8	12
Settlement and curtailment losses	13	--	13	--
Contributions to multiemployer pension plans	2	3	5	5
<b>Net periodic pension cost</b>	<b>\$ 56</b>	<b>\$ 56</b>	<b>\$ 99</b>	<b>\$ 112</b>

The net periodic pension cost above includes approximately \$1 million for the second quarter of 2003 and \$1 million and \$2 million for the first six months of 2004 and 2003, respectively, reported as discontinued operations.

Through July 3, 2004, we recognized \$99 million of pension expense. We anticipate recording an additional \$89 million of pension expense in the remainder of 2004 for a total of \$188 million, which includes settlement and curtailment losses of \$13 million related to the second-quarter 2004 sales of our building products distribution segment and our non-integrated pulp mills. The \$19 million reduction in expected expense for the year is primarily related to the remeasurement of our salaried pension plan in connection with the sales of our building products distribution segment and our non-integrated pulp mills.

Through July 3, 2004, we made pension contributions of \$107 million. We presently anticipate contributing an additional \$100 million to fund our pension plans in the remainder of 2004 for a total of \$207 million for 2004.

#### Health Care and Life Insurance Benefits

The majority of our retiree medical plans provide prescription drug benefits that will be affected by the Medicare Prescription Drug, Improvement, and Modernization Act of 2003 ("the Act"), signed into law in December 2003. In accordance with FSP FAS 106-2, *Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003*, we have included the effects of the Act on our medical plans retroactively in the second quarter of 2004. The reduction in our accumulated postretirement benefit obligation attributed to past service is approximately \$67 million. The impact of the subsidy on net periodic postretirement benefit cost for the current period is a reduction in the interest cost on the accumulated postretirement benefit obligation of approximately \$1 million and the

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elimination of our requirement to amortize unrecognized gains or losses. The required amortization would have been approximately \$1 million.

Net periodic postretirement benefit cost during the second quarters and first six months of 2004 and 2003 included the following components:

(In millions)	Second Quarter		First Six Months	
	2004	2003	2004	2003
Service cost of benefits earned	\$ 1	\$ 1	\$ 2	\$ 3
Interest cost on accumulated	9	11	19	22



postretirement benefit obligation	(5)	(3)	(9)	(5)
Amortization of prior service credit	--	--	1	--
Amortization of unrecognized loss				
<b>Net periodic postretirement benefit cost</b>	<b>\$ 5</b>	<b>\$ 9</b>	<b>\$ 13</b>	<b>\$ 20</b>

12. **COMMITMENTS AND CONTINGENCIES.** We are involved in various legal proceedings incidental to our business and are subject to a variety of environmental and pollution control laws and regulations in all jurisdictions in which we operate. As is the case with other companies in similar industries, Georgia-Pacific faces possible liabilities, and defense costs, from actual or potential claims and legal proceedings involving a wide variety of issues.

#### ENVIRONMENTAL MATTERS

We are involved in environmental remediation activities at approximately 173 sites, both owned by us and owned by others, where we have been notified that we are or may be a potentially responsible party ("PRP") under the United States Comprehensive Environmental Response, Compensation and Liability Act ("CERCLA") or similar state "superfund" laws. Of the known sites in which we are involved, we estimate that approximately 43% are being investigated, approximately 20% are being remediated and approximately 37% are being monitored (an activity that occurs after either site investigation or remediation has been completed). The ultimate costs to us for the investigation, remediation and monitoring of many of these sites cannot be predicted with certainty, due to the often unknown nature and magnitude of the pollution or the necessary cleanup, the varying costs of alternative cleanup methods, the amount of time necessary to accomplish the cleanups, the evolving nature of cleanup technologies and governmental regulations, and the inability to determine our share of multiparty cleanups or the extent to which contribution will be available from other parties, all of which factors are taken into account to the extent possible in estimating our liabilities. We have established reserves for environmental remediation costs for these sites that we believe are probable and reasonably able to be estimated. To the extent that we are aware of unasserted claims, consider them probable, and can estimate their potential costs, we include appropriate amounts in the reserves.

Based on analyses of currently available information and previous experience with respect to the cleanup of hazardous substances, we believe it is reasonably possible that costs associated with these sites may exceed current reserves by amounts that may prove insignificant or that could range, in the aggregate, up to approximately \$129 million. This estimate of the range of reasonably possible additional costs is less certain than the estimates upon which reserves are based, and in order to establish the upper limit of this range, assumptions least favorable to us among the range of reasonably possible outcomes were used. In estimating both our current reserve for environmental remediation and the possible range of additional costs, we have not assumed we will bear the entire cost of remediation of every site 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, based generally on their financial condition and probable contribution on a per-site basis.

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Presented below is the activity in our environmental liability account for the last three fiscal years and first six months of 2004 and 2003.

In millions	First Six Months		Fiscal Year Ended		
	2004	2003	2003	2002	2001
Beginning balance	\$ 230	\$ 306	\$ 306	\$ 318	\$ 121
Expense charged to earnings:					
Related to previously existing matters	2	--	(64)	14	2
Related to new matters	5	--	1	--	15
Amounts related to acquisitions:	--	--	--	--	207
Purchase price allocations	7	(3)	(4)	--	--
Reclassification of reserves	(5)	(6)	(9)	(26)	(27)
Payments					
Ending balance	\$ 239	\$ 297	\$ 230	\$ 306	\$ 318

#### KALAMAZOO RIVER SUPERFUND SITE

We are currently implementing an Administrative Order by Consent ("AOC") entered into with the Michigan Department of Natural Resources and the United States Environmental Protection Agency ("United States EPA") regarding an investigation of the Kalamazoo River Superfund Site. The Kalamazoo River Superfund Site is comprised of 35 miles of the Kalamazoo River, three miles of Portage Creek and a number of operable units in the form of landfills, waste disposal areas and impoundments. We became a PRP for the site in December 1990 by signing the AOC. There are two other named PRPs at this time. The contaminant of concern is polychlorinated biphenyls ("PCBs") in the river sediments and residuals in the landfills and waste disposal areas.

A draft Remedial Investigation/Feasibility Study ("RI/FS") for the Kalamazoo River was submitted to the State of Michigan on October 30, 2000 by us and other PRPs. The draft RI/FS evaluated five remedial options ranging from no action to total dredging of the river and off-site disposal of the dredged materials. In February 2001, the PRPs, at the request of the State of Michigan, also evaluated 9 additional potential remedies. The cost for these remedial options ranges from \$0 to \$2.5 billion. The draft RI/FS recommends a remedy involving stabilization of over twenty miles of riverbank and long-term monitoring of the riverbed. The total cost for this remedy is approximately \$73 million. It is unknown over what timeframe these costs will be paid out. The United States EPA has taken over management of the RI/FS and is evaluating the proposed remedy. We cannot predict what impact or change will result from the United States EPA's assuming management of the site.

We are paying 45% of the costs for the river portion of the RI/FS investigation based on an interim allocation. This 45% interim allocation includes the share assumed by Fort James prior to its acquisition by us. Several other companies have been identified by government agencies as PRPs, and all but one is believed to be financially viable.

As part of implementing the AOC, we have investigated the closure of two disposal areas which are contaminated with PCBs. The cost to remediate one of the disposal areas, the King Highway Landfill,

was approximately \$9 million. The remediation of that area is essentially complete and we are waiting for final approval of the closure from the State of Michigan. A 30-year post-closure care period will begin upon receipt of closure approval, and over that period we will make expenditures accrued for post-closure care. We are solely responsible for closure and post-closure care of the King Highway Landfill.

It is anticipated that the cost for closure of the second disposal area, the Willow Boulevard/A Site landfill, will be approximately \$8 million. The State of Michigan has drafted a new RI/FS for this landfill and we are in the process of preparing comments on that document. The new draft RI/FS evaluates the same remedies proposed by the PRPs. The decision as to the actual remedy will be made by the United States

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EPA after the RI/FS is finalized, which is expected to be this year. We believe the United States EPA will require a remedy for this landfill similar to the King Highway landfill closure. It is anticipated these costs will be paid out over the next five years, and costs for post-closure care for 30 years following certification of the closure. We are solely responsible for closure and post-closure care of the Willow Boulevard portion of the landfill, and are sharing investigation costs for the A Site portion of the landfill with Millennium Holdings on an equal basis. A final determination as to how closure and post-closure costs for the A Site will be allocated between us and Millennium Holdings has not been made; however, our share should not exceed 50%.

We have spent approximately \$34.0 million on the Kalamazoo River Superfund Site through July 3, 2004 broken down as follows:

<u>Site</u>	<u>(in millions)</u>
River	\$ 19.7
King Highway	9.3
A Site	2.0
Willow Blvd.	<u>3.0</u>
	<u>\$ 34.0</u>

All of these amounts were charged to earnings.

The reserve for the Kalamazoo River Superfund Site is based on the assumption that the bank stabilization remedy will be selected as the final remedy by the United States EPA and the State of Michigan, and that the costs of the remedy will be shared by several other PRPs.

#### FOX RIVER SUPERFUND SITE

The Fox River site in Wisconsin is comprised of 39 miles of the Fox River and Green Bay. The site was nominated by the United States EPA (but never finally designated) as a Superfund site due to contamination of the river by PCBs through wastewater discharged from the recycling of carbonless copy paper from 1953-1971. We became a PRP through our acquisition of Fort James.

In late July of 2003, the Wisconsin Department of Natural Resources ("WDNR") and the United States EPA issued a Record of Decision ("ROD") for Operable Units ("OU") 3, 4 and 5 of the Fox River. OU 3 is the section of the Fox River running downstream from Little Rapids to the De Pere dam, and Operable Unit 4 runs from the De Pere dam downstream to the mouth of the Fox River at Green Bay. Operable Unit 5 is Green Bay. The Fort James facility, which potentially discharged PCBs, is located in OU 4 approximately 3 miles downstream from the De Pere dam.

The ROD calls for the removal by dredging of all sediments in OUs 3 and 4 containing PCBs above one part per million. The amount of sediment estimated to contain PCBs above one part per million is 586,800 cubic yards in OU 3 and 5,880,000 cubic yards in OU 4. The ROD also calls for monitored natural recovery for OU 5. The ROD estimates the dredging remedy for OUs 3 and 4 and the monitored natural recovery for OU 5 will cost \$324 million. However, the ROD does allow for capping as an alternative remedy to dredging in certain areas of OUs 3 and 4 if capping would be less costly than dredging and provide the same level of protection as dredging. The WDNR estimated that approximately 40% of the total volume of contaminated sediments in OUs 3 and 4 would be eligible for capping based upon the capping criteria defined in the ROD. The allowance for capping in the ROD represents a major change from the proposed remedial action plan issued by WDNR in 2001, which did not provide or allow for capping in any areas of OUs 3 and 4.

Six other companies have been identified by the governments as PRPs. Under an interim allocation agreement, we were paying 30% of costs incurred by the PRPs in analyzing and responding to all of the governmental documents which preceded the issuance of the ROD. With the issuance of the ROD, we do not anticipate that the PRPs will be engaged in any further formal work as a group. We believe that all of

the PRPs are liable for some portion of the costs of remediating OUs 4 and 5, and that our ultimate liability will be less than 30% of the total estimated cost of remediating the Fox River site.

Following issuance of the ROD we analyzed its remedial provisions as well as the relevant facts impacting our potential liability. We concluded that we will be able to utilize the capping remedy to the extent permitted by the ROD. We also concluded that there are geographic limitations on our potential liability, and that we can limit our responsibility for the removal and capping of PCBs to the part of OU 4 immediately adjacent to and downstream from the Fort James facility in Green Bay, Wisconsin. We share liability for any appropriate monitoring in OU 5 with all of the PRPs. Based on these considerations we determined that we would not be required to utilize all of the reserve previously established for this site, and in December, 2003 reduced such reserve by approximately \$66 million.

We have spent approximately \$38 million from 1995 to July 3, 2004 on the Fox River site, some of which was spent by Fort James prior to its acquisition by us.

Along with another PRP, we have entered into an Administrative Order on Consent ("AOC") to prepare the remedial design for OUs 3, 4 and 5. We are presently developing a work plan for the design effort and expect to conduct pre-design sampling in OUs 3, 4 and 5 this summer.

In 2002, we entered into an agreement with the WDNR and the United States Fish and Wildlife Service to settle claims for natural resource damages under CERCLA, the Federal Water Pollution Control Act and state law for approximately \$12 million, and to date have paid approximately \$9 million of this amount. The agreement was entered by the Federal District Court in Wisconsin on March 19, 2004 and is now effective. The \$12 million to be paid under this agreement is separate and apart from any costs related to remediation of the Fox River site.

In 1999 we and Chesapeake Corporation formed a joint venture to which a Chesapeake subsidiary, Wisconsin Tissue Mills, Inc., contributed tissue mills and other assets located along the Fox River. Wisconsin Tissue is one of the PRPs for the Fox River site. Chesapeake and Wisconsin Tissue specifically retained all liabilities arising from Wisconsin Tissue's status as a PRP, and indemnified the joint venture and us against these liabilities. In 2001, we (having acquired all of Chesapeake's interest) sold this joint venture to Svenska Cellulosa Aktiebolaget (publ) ("SCA") and indemnified SCA and the joint venture against all environmental liabilities (including all liabilities arising from the Fox River site for which Wisconsin Tissue is ultimately responsible) arising prior to the closing of the SCA sale. As part of the agreement pursuant to which we acquired Chesapeake's interest in the joint venture, Chesapeake specifically agreed that we would retain Chesapeake's prior indemnification for these liabilities.

#### WHATCOM WATERWAY SUPERFUND SITE

The Whatcom Waterway is a Federal channel located adjacent to our facilities in Bellingham, Washington. The State of Washington declared the Whatcom Waterway a Superfund site due to historical contamination of sediments with woody debris, phenolics and mercury. On March 6, 1995, the Washington Department of Ecology named us as a Potentially Liable Party ("PLP") in the case. The State is presently preparing to name other PLPs in the case.

We completed an RI/FS and identified a preferred remedial alternative comprised of a combination of dredging, capping and habitat restoration with a total estimated cost of \$23 million. It is anticipated these costs will be paid out over the next 5 to 10 years. We have completed interim remedial action and habitat restoration of a portion of the site. Environmental monitoring of this portion of the site is ongoing. The reserve for the Whatcom Waterway site is based on the assumptions that the \$23 million proposed remedy involving limited dredging and capping will be selected by the State of Washington as the final remedy and that the cost of the remedy will be shared among a small group of PLPs. We have spent approximately \$3.6 million through July 3, 2004 on the Whatcom Waterway site, all of which was charged to earnings.

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In June of 2004, we signed a letter of intent with the Bellingham Port Authority (the "Port") to sell our Bellingham facilities to the Port and lease back certain of those facilities. The Port will assume our

responsibility for all environmental liabilities associated with the facility. Assuming the parties reach a formal agreement for this transaction, we expect closing to occur in the fourth quarter of 2004.

## ASBESTOS LITIGATION

We and many other companies are defendants in suits brought in various courts around the nation by plaintiffs who allege that they have suffered personal injury as a result of exposure to asbestos-containing products. Our asbestos liabilities relate primarily to joint systems products manufactured by Bestwall Gypsum Company and our gypsum business that contained small amounts of asbestos fiber. We acquired Bestwall in 1965, and discontinued using asbestos in the manufacture of these products in 1977.

### Pending Claims

These suits allege a variety of lung and other diseases based on alleged exposure to our products. In many cases, the plaintiffs are unable to demonstrate that they have suffered any compensable loss as a result of such exposure, or that any injuries they have incurred did in fact result from exposure to our products. Virtually all asbestos suits involve multiple defendants and seek money damages. We are unable to provide any meaningful disclosure about the total amount of such damages, for the following reasons:

We do not track this data in any form since we do not consider the amount of damages, if any, alleged in the initial complaint relevant in assessing our exposure to asbestos liabilities;

In the past, we estimated that less than 15% of the claims then pending against us contained any specific demand for damages, as opposed to a general demand for such damages as the plaintiff may prove at trial, or a demand which was stated as being in excess of the minimum jurisdictional limit of a particular court;

Those complaints which did contain a specific damage demand nearly always involved multiple defendants (anywhere from 30 to over 100), most of which never manufactured joint systems products. In this review, we did not identify any complaint which stated a specific demand for money damages solely from us;

Claims which did allege specific damages often alleged the same amount of damages regardless of the specific disease a plaintiff may have had. In addition, in many such cases no specific disease was alleged, and thus the damages alleged were meaningless because the ultimate settlement value of any claim is significantly influenced by the actual disease the plaintiff is able to prove; and

Because we do not track this data and do not consider the amount of damages, if any, alleged in the initial complaint relevant in assessing our exposure to asbestos liabilities, we have not updated this analysis and do not intend to do so in the future.

The following table presents information about the approximate number of our asbestos claims during the past three fiscal years and the first six months of each of 2004 and 2003:

	<u>First Six Months</u>		<u>Fiscal Year Ended</u>		
	<u>2004</u>	<u>2003</u>	<u>2003</u>	<u>2002</u>	<u>2001</u>
Claims Filed <sup>1</sup>	19,900	29,500	39,000	41,700	39,700
Claims Resolved <sup>2</sup>	20,500	31,200	43,500	35,100	30,900
Claims Unresolved at End of Period	63,700	67,100	64,300	68,800	62,200

1 Claims Filed includes all asbestos claims for which service has been received and/or a file has been opened by us and each such claim represents a plaintiff who is pursuing an asbestos claim against us.

2 Claims resolved include asbestos claims which have been settled or dismissed or which are in the process of being settled or dismissed based upon agreements or understandings in place with counsel for the claimants.

In addition, Fort James Corporation, one of our wholly-owned subsidiaries, currently is defending approximately 780 asbestos premises liability claims.

#### Asbestos Liabilities

From the commencement of this litigation through July 3, 2004, we either had settled, had dismissed or were in the process of settling a total of approximately 333,700 asbestos claims. For this same period our asbestos payments, for liability, defense and administration, before insurance recoveries and tax benefits, totaled approximately \$725 million. We generally settle asbestos claims for amounts we consider reasonable given the facts and circumstances of each claim.

In the fourth quarter of 2001, we recorded a pre-tax charge to earnings of \$350 million to cover the probable and reasonably estimable asbestos liabilities and defense costs we believed we would pay through 2011, net of expected insurance recoveries during this same period. The charge was based on projections prepared by National Economic Research Associates (NERA) and Navigant Consulting (formerly known as Peterson Consulting), nationally recognized firms with expertise in asbestos liability and insurance coverage matters, and contained many assumptions. NERA's projection of our future asbestos liabilities assumed that beginning in 2001 the number of new claims filed against us for asbestos-related injuries would decline at a fairly constant rate each year through 2011. It also assumed that we would pay about \$105 million for our asbestos liabilities and defense costs in 2002 (compared to about \$84 million in 2001), with such payments then declining at varying rates over the period through 2011.

In fact, during 2002 the number of new claims filed against us increased somewhat and

our total asbestos liabilities and defense costs were approximately \$75 million more than NERA's projection had assumed. This result was due principally to higher settlement costs in 2002 for claims involving mesothelioma, which represent a very small percentage of our total asbestos claims but accounted for well over half of our total asbestos liabilities in 2002. In addition, during 2001 a number of other manufacturers of asbestos-containing products, including one of our principal competitors in the manufacture of joint systems products, filed for bankruptcy. During 2002 many plaintiff lawyers increased their settlement demands on us, principally in mesothelioma cases, to compensate for these bankruptcies. As a result, at the end of 2002 NERA increased its original estimate of our asbestos liabilities and defense costs over the period through 2011, and extended the projection through 2012, to a total of slightly less than \$1.2 billion, before any insurance recoveries and ignoring possible tax benefits. In the fourth quarter of 2002 we recorded an additional pre-tax charge to earnings of \$315 million which, when added to amounts remaining from the charges recorded in 2001, we believed were sufficient to cover our projected asbestos liabilities and defense costs, net of expected insurance recoveries, through 2012.

During 2003 we observed a number of developments involving our asbestos litigation, including the following:

The total number of new claims filed in 2003 was slightly below 2002 levels; the rate of such filings peaked in the second quarter and then declined sharply in the third and fourth quarters. The peak in the second quarter was due primarily to the passage of tort reform legislation in Mississippi, which became effective at the end of 2002 and which resulted in a large number of claims being filed in Mississippi by plaintiff's lawyers seeking to ensure their claims would be governed by the law in effect prior to passage of tort reform.

The United States Senate Judiciary Committee passed a bill that would establish a trust fund to pay future asbestos-related disease claims and remove such cases from federal and state courts, with industry and insurers funding the trust with payments estimated to total about \$114 billion over a 50-year period; the legislation reflected widespread concern over the inability of courts to deal fairly and efficiently with asbestos claims and the fact that 50-60% of total asbestos payments in the United States represent legal fees and related costs.

Tort reform legislation was enacted in Arkansas, Mississippi, Ohio, Texas and West Virginia, which are states that together account for a significant number of the asbestos claims pending against us; the effect of such legislation cannot be assessed yet.



For 2003, our total payments for asbestos liabilities and defense costs (before insurance and tax benefits) were \$189 million. NERA has reviewed our 2003 asbestos liability and defense cost payments and compared them to the revised estimate it made at the end of 2002. Based on this review, NERA concluded that the 2003 payments were in line with its revised estimate and that the assumptions it used in that estimate remain valid. Accordingly, the only adjustment to our asbestos reserve in 2003 was to accrue an additional amount equal to payments we anticipate making in 2013 for asbestos liabilities and defense costs, so that the reserve remains a ten-year reserve. NERA estimated this amount to be \$54 million (before insurance and tax benefits). Accordingly, in the fourth quarter of 2003 we recorded a pre-tax charge of \$54 million to record this additional accrual. We believe that NERA's projection for 2004 through 2013 represents the best estimate of the reasonably estimable asbestos costs we will incur based upon currently available information.

On April 22, 2004, the United States Senate voted on a bill, which was substantially similar to the bill described above that was passed by the United States Senate Judiciary Committee in 2003. The vote, on a motion to impose cloture on the debate surrounding the bill, was 50-47; 60 votes were required to impose cloture. Cloture is a procedural step to limit debate on a bill. Following that vote the leaders of both political parties in the U.S. Senate have led ongoing negotiations among industry, insurers, labor unions and other interested parties to revise this bill so that it would be acceptable to all parties. It is possible that the Senate will vote on a revised bill in September, but enactment of such legislation is uncertain.

#### Insurance

In 2001, 2002 and again in 2003, we, with advice from legal counsel and Navigant Consulting, also reviewed our existing insurance policies, analyzed publicly available information bearing on the creditworthiness of our various insurers, and employed insurance allocation methodologies which we and our advisors considered appropriate to ascertain the amount of probable insurance recoveries from our insurers for our present and future asbestos liabilities. Assumptions were made about self-insurance reserves, policy exclusions, liability caps and gaps in our coverage, the resolution of allocation issues among various layers of insurers, as well as insolvencies of certain of our insurance carriers and the continued solvency of our other insurers. Based on this analysis, Navigant Consulting projected our expected insurance recoveries for asbestos liabilities and costs over the period through 2013.

During 2003 we entered into agreements with several of our insurers to confirm amounts payable by them under applicable policies. These agreements generally provide that we will be able to recover more

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insurance than we had assumed when we were projecting our insurance receivables in 2001 and 2002. During 2003 we revised our insurance receivable to include recoveries under these agreements, to account for favorable negotiations and other recoveries from certain other insurers, to change our allocation methodology for remaining solvent insurers consistent with these agreements, and to reflect possible insolvencies at two of our insurers. The net effect of these changes was to increase our total insurance receivable by \$156 million during 2003. All of our available insurance is included in our insurance receivable.

The insurance receivables recorded by us do not assume any recovery from insolvent carriers, and assume that those carriers which are currently solvent will continue to be solvent. However, there can be no assurances that these assumptions will be correct. Substantially all of the insurance recoveries deemed probable are from insurance companies rated A- (excellent) or better by A.M. Best Company. No more than 33% of such insurance recoveries are from any one company, though several of the insurers are under common control.

In the fourth quarter of 2003, we sold without recourse approximately \$156 million of our insurance receivables, representing claims already paid by us to a third party, for approximately \$147 million in cash.

### Key Assumptions

The analyses and projections of NERA and Navigant Consulting are based on their professional judgment. The more important assumptions in NERA's projection of the number of claims that will be filed against us include the population potentially exposed to asbestos-containing products manufactured by us, the expected occurrence of various diseases in these potentially exposed populations, the rate at which these potentially exposed populations actually file claims, and activities of the asbestos plaintiffs bar designed to maximize its profits from such claims. The cost of settling claims is driven by these same assumptions, as well as by prevailing judicial and social environments in the jurisdictions in which claims are filed, the rulings by judges and the attitudes of juries in respect to the value of each such claim, the insolvencies of other defendants to a particular claim, and the impact of verdicts against other defendants on settlement demands against us.

Generally, NERA's projections assume:

That the number of new claims to be filed against us each year through 2013 will decline at a fairly constant rate each year beginning in 2003;

That the percentage of claims settled by us will be about three-quarters of the total number of claims resolved (whether by settlement or dismissal) each year through 2013;

That the average estimated per case settlement costs are anticipated to decrease slightly over the period through 2013; and

That the total amount paid by us in settlements, and in defense and administrative costs, will decline at varying rates over the period through 2013

Among the more important assumptions made by Navigant Consulting in projecting our future insurance recoveries are the resolution of allocation issues among various layers of insurers, the application of particular theories of recovery based on decided cases, and the continuing solvency of various insurance companies.

Given these assumptions and the uncertainties involved in each of them, our actual asbestos liabilities, defense costs and insurance recoveries could be higher or lower than those currently projected and/or

recorded. However, these assumptions are only some of those contained in the NERA and Navigant Consulting projections, and all of such assumptions are only one aspect of the overall projections made by those firms. Changes in the foregoing assumptions, or others, whether from time to time or over the period covered by such projections, may or may not affect the validity of the overall projections. We intend to monitor our accrued asbestos liabilities, defense costs and insurance recoveries against these overall

projections, and will make adjustments to such accruals as required by generally accepted accounting principles.

#### Summary of Accruals

In the fourth quarter of 2003 we recorded a net pre-tax charge to earnings of \$16 million, which when added to our existing reserves are estimated to cover the probable and reasonably estimable asbestos liabilities and defense costs we believe we will pay through 2013, net of expected insurance recoveries during this same period. The following table summarizes accruals to, and payments from, our reserve for our total asbestos personal injury liabilities, receipts from our insurance carriers, including the monetization of a part of such receivables in 2003 as described above, and other changes to our expected insurance receivables, for the last three fiscal years and first six months of each of 2004 and 2003 (dollars in millions):

	First Six Months		Fiscal Year End		
	2004	2003	2003	2002	2001
Asbestos Liabilities					
	\$ 1,027	\$ 1,162	\$ 1,162	\$ 836	\$ 136
	--	--	54	507	784
Beginning Balance			(189)	(181)	(84)
Accruals					
Payments	(95)	(89)			
Ending Balance	\$ 932	\$ 1,073	\$ 1,027	\$ 1,162	\$ 836
Insurance Receivable					
	\$ 576	\$ 669	\$ 670	\$ 527	\$ 172
	--	--	156	192	421
Beginning Balance	(18)	(74)	(250)	(49)	(66)
Accruals					
Receipts					
Ending Balance	\$ 558	\$ 595	\$ 576	\$ 670	\$ 527

The amounts accrued for asbestos liabilities are recorded under "Other current liabilities" and "Other long-term liabilities," and the amounts accrued for insurance receivables are reflected under "Other current assets" and "Other assets," in the accompanying consolidated balance sheets.

During the first half of 2004 the number of new asbestos claims filed against us decreased 32% compared to the first half of 2003. Our payments to settle pending asbestos cases were approximately equal to our projections for the period and equal to the amount paid in the first six months of 2003. However, defense costs over the past several quarters were significantly higher than projected, and are expected to remain at their current level for an unknown period of time. Defense costs have increased as we have undertaken more discovery with regard to the medical condition and allegations of causation of plaintiffs who allege malignant conditions. Additionally, we have taken more cases to trial. We are monitoring the amount of future defense costs projected to be incurred and the potential impact of such costs on our settlement projections and the asbestos reserves.

There can be no assurance that our currently accrued asbestos liabilities will be sufficient to cover our payments for such liabilities and related defense costs, or that our accrued insurance recoveries will be realized, through 2013. We believe that it is reasonably possible that we will incur additional charges for our asbestos liabilities and defense costs in the future which could exceed our existing reserves, but cannot estimate such excess amount at this time. We also believe that it is reasonably possible that such excess liabilities could be material to our operating results in any given quarter or year but, based on the information available to us at present, do not believe that it is reasonably possible that such excess liabilities would have a material adverse effect on our long-term results of operations, liquidity or consolidated financial position.

## OTHER LITIGATION

In late December 2003, we settled all claims in a class action lawsuit filed against us and the Georgia-Pacific Corporation Salaried Employees Retirement Plan (the "Plan") in 1997 seeking recovery of alleged underpayments of lump-sum benefits to persons taking early retirement. In May 2004, the district court approved the settlement and dismissed with prejudice all claims against the Plan and us. Under the settlement the Plan will pay \$67 million in additional benefits to certain class members plus 1% simple annual interest from December 18, 2003 until the date of distribution, which includes attorney and class representative fees, and costs to administer the settlement. The settlement amount has been included in our projected benefit obligation, and is not expected to have a material impact on our funding obligations or results of operations.

In 2003, we settled a class action antitrust lawsuit filed against us and other manufacturers of containerboard. However, a significant number of plaintiffs opted out of the class and brought suit against the same defendants, making substantially the same allegations. During the first half of 2004, we recorded a pre-tax charge of \$6 million for the settlement of these lawsuits. We have resolved all but one of these opt out cases.

In August 1995, Fort James, at the time a publicly-held corporation, transferred certain assets and liabilities of its communications paper and food packaging businesses to two newly formed companies, Crown Vantage, Inc. ("CV"), (a wholly-owned subsidiary of Fort James) and CV's subsidiary Crown Paper Co. ("CP"). CP then entered into a \$350 million credit facility with certain banks and issued \$250 million face amount of senior subordinated notes. Approximately \$483

million in proceeds from these financings were transferred to Fort James in payment for the transferred assets and other consideration. CV also issued to Fort James a pay-in-kind note with a face amount of \$100 million. CV shares were then spun off to the Fort James shareholders and CV operated these businesses as a stand-alone company beginning in August 1995.

In March 2001, CP and CV filed for bankruptcy. Various creditors have alleged that the borrowings made by CP and CV, and the payments to Fort James for the assets transferred to CV and CP, caused those companies to become insolvent, and that the transfer of these assets therefore was a fraudulent conveyance. In April 2001, Fort James filed suit against CP and CV in Federal Bankruptcy Court in Oakland, California seeking a declaratory judgment that the transactions did not involve any fraudulent conveyance and that other parties and actions were the cause of the bankruptcy of CV and CP. In September 2001, CV filed suit in Federal District Court in San Francisco against Fort James asserting, among other claims, that the transactions described above constituted fraudulent conveyances and seeking unspecified damages. Early in July 2004 that court in San Francisco dismissed a number of these claims, and continued proceedings with respect to two remaining claims. It had earlier lifted an injunction imposed by the Federal Bankruptcy Court in Oakland which prevented us from proceeding with an action we filed in Delaware that asserts that a 1998 agreement released all claims by CV and CP against Fort James. CV and CP have appealed the order lifting this injunction. Fort James does not believe that any of its actions in establishing CV or CP involved a fraudulent conveyance or caused the bankruptcy of those companies, and it intends to defend itself vigorously.

The Wisconsin Department of Natural Resources ("WDNR") has referred a Notice of Violation ("NOV") to the Wisconsin Department of Justice ("WDOJ") for further action. The NOV alleges violations by one of our Green Bay paper mills of certain air regulations and permitting requirements concerning emissions from the mill's printing operations and emission monitoring requirements for the mill's dry forming operations. The Company discovered and voluntarily disclosed to WDNR the facts underlying both sets of allegations. This matter has been settled for \$95,000.

Although the ultimate outcome of these environmental matters and legal proceedings cannot be determined with certainty, based on presently available information management believes that adequate reserves have been established for probable losses with respect thereto. Management further believes that the ultimate outcome of these and other environmental matters and legal proceedings could be material to operating

results in any given quarter or year but will not have a material adverse effect on our long-term results of operations, liquidity or consolidated financial position.

#### GUARANTEES AND INDEMNIFICATIONS

Georgia-Pacific is a party to contracts in which it is common for us to agree to indemnify third parties for certain liabilities that arise out of or relate to the subject matter of the contract. In some

cases, this indemnity extends to related liabilities arising from the negligence of the indemnified parties, but usually excludes any liabilities caused by gross negligence or willful misconduct. We cannot estimate the potential amount of future payments under these indemnities until events arise that would trigger a liability under the indemnities.

We are a 50% partner in a joint venture ("GA-MET") with Metropolitan Life Insurance Company ("Metropolitan"). GA-MET owns and operates our main office building in Atlanta, Georgia. We account for the investment in GA-MET under the equity method. At July 3, 2004, GA-MET had an outstanding mortgage loan payable to Metropolitan in the amount of \$125 million. The note bears interest at 9.5%, requires monthly payments of principal and interest through 2011, and is secured by the land and building owned by the joint venture. In the event of foreclosure, each partner has severally guaranteed payment of one-half of any shortfall of collateral value to the outstanding secured indebtedness. Based on present market conditions and building occupancy, the likelihood of any obligation to us with respect to this guarantee is considered remote.

Additionally, in connection with the sale of assets and the divestiture of businesses, we may agree to indemnify the buyer of the assets and related parties for certain losses or liabilities incurred by the buyer with respect to (i) the representations and warranties made by us to the buyer in connection with the sale and (ii) liabilities related to the pre-closing operations of the assets sold. Indemnities related to pre-closing operations generally include environmental liabilities, tax liabilities, and other liabilities not assumed by the buyer in the transaction.

Indemnities related to the pre-closing operations of sold assets normally do not represent additional liabilities to us, but simply serve to protect the buyer from potential liability associated with our obligations existing at the time of the sale. As with any liability, we have previously accrued for those pre-closing obligations that are considered probable and reasonably estimable. We have not accrued any additional amounts as a result of the indemnities summarized below, which result from significant asset sales and divestitures in recent years.

- SCA

-- In connection with the sale of our away-from-home tissue manufacturing assets to SCA, we agreed to indemnify SCA with respect to certain losses resulting from breaches of our representations and warranties contained in the sale agreement. We are not required to pay under this general indemnification obligation until claims against us, on a cumulative basis, exceed \$2 million. Upon exceeding this \$2 million threshold, we generally are obligated to provide indemnification for any losses in excess of \$1 million, up to a limit of \$425 million. The majority of these general indemnification obligations expired on March 2, 2003, and SCA has asserted some claims under these provisions. However, we remain subject to certain claims by SCA for various environmental claims until early 2009. Unlike our \$425 million limit on liability with respect to general claims, our liability with respect to certain environmental claims made by SCA is capped at \$850 million, less the amount of any indemnification payments previously made under our general indemnification obligations.

- Domtar Inc.

-- In connection with the sale of certain of our paper and pulp mills to Domtar, we agreed to indemnify Domtar for certain losses resulting from breaches of our representations and warranties

contained in the sale agreement. We are not required to pay under this general indemnification obligation until claims against us, on a cumulative basis, exceed \$16 million. Upon exceeding this \$16 million threshold, we generally are obligated to provide indemnification for any losses in excess of \$16 million, up to a limit of \$500 million. The majority of these general indemnification obligations expired on March 31, 2003, and Domtar has asserted some claims under these provisions. However, we remain subject to certain claims by Domtar for various environmental liabilities assumed by it until mid-2011. Our liability with respect to these environmental claims is capped at \$100 million, and is subject to the \$16 million threshold discussed above.

- Plum Creek

-- In connection with the merger of our timberlands business into Plum Creek, we agreed to indemnify Plum Creek with respect to certain losses resulting from breaches of limited representations and warranties contained in the separation agreement. This indemnity generally is not capped at a maximum potential liability and does not expire, but we believe we have very limited exposure under it.

- Unisource

-- In connection with the sale of 60% of our Unisource paper distribution subsidiary to an affiliate of Bain Capital Partners, LLC, we agreed to indemnify Unisource for certain losses resulting from breaches of our representations and warranties contained in the sale agreement. We are not required to pay under this general indemnification obligation until claims against us, on a cumulative basis, exceed \$8 million. Upon exceeding this \$8 million threshold, we are generally obligated to provide indemnification for any losses in excess of \$8 million, up to a limit of \$150 million. This general indemnification obligation expires on May 2, 2005, provided that Unisource may make certain claims with respect to various (i) tax and employee benefit matters until the expiration of the applicable statute of limitations and (ii) environmental matters until late 2007.

- Norampac, Inc.

-- As part of an asset exchange with Norampac, we agreed to indemnify Norampac with respect to any losses resulting from (i) the breach of limited representations and warranties contained in the asset exchange agreement, (ii) any pre-exchange liabilities related to the exchanged facility not assumed by Norampac, and (iii) any environmental liability related to the pre-exchange operations of the exchanged facility. We are not required to pay under this general indemnification obligation until claims against us, on a cumulative basis, exceed \$500,000. Upon exceeding this threshold, we generally are obligated to provide indemnification for any losses in excess of \$500,000, up to a limit of \$10 million. The majority of these general indemnification obligations and the environmental liability indemnity expire in April 2006.

- Genessee & Wyoming Inc.

-- In connection with the sale of the assets of certain of our railroads to Genessee & Wyoming Inc. ("GWI"), we agreed to indemnify GWI for certain losses suffered as a result of our breaches of certain representations, warranties and covenants contained in the sale agreement. We are generally not required to pay under the indemnities until claims against us, on a cumulative basis, exceed \$500,000. Upon exceeding this threshold, we are generally obligated to provide indemnification for losses in excess of \$500,000, up to a limit of \$20 million for general indemnities. With respect to our environmental indemnities generally, we are obligated to provide indemnification for 80% of

losses in excess of \$500,000 and GWI is responsible for the remaining 20%, up to a total cap of \$2 million. In the event environmental liabilities exceed \$2 million, we are obligated to pay 100% of any such excess up to a limit of \$15 million. The majority of these general indemnification obligations expire in June 2005, while the environmental liability indemnity expires in December 2008.

- Sale of Insurance Receivables.

-- In 2003, we sold, without recourse, approximately \$156 million of asbestos insurance receivables to a trust established for the purpose of securitizing the receivables. We have retained no interests in the trust or the receivables. According to the sale agreement, the Certificate of Claims Qualification and Qualified Payments have been transferred to the purchaser. Our continuing involvement is limited to our agreement to indemnify the trust for any losses resulting from our breach of any representation or warranty we made in agreements associated with the sale, or any claims brought by the insurance companies.

- Building Products Distribution

- In connection with the sale of our building products distribution business to Cerberus Capital Management L.P. ("Cerberus") in 2004, we agreed to indemnify Cerberus for certain losses incurred as a result of breaches of certain representations, warranties and covenants made by us contained in the sale agreement. We are generally not required to pay under the indemnities until claims against us, on a cumulative basis, exceed \$7 million. Upon exceeding this threshold, we are generally obligated to provide indemnification for losses up to an aggregate of 15 percent of the purchase price or approximately \$120 million. The majority of these indemnities expire in May 2006 while some expire in May 2010. We have also agreed to indemnify Cerberus for certain pre-closing environmental and product liability claims, without the application of deductibles or caps. Although our indemnity for these pre-closing environmental and product liability claims does not expire, we believe we have limited exposure under this indemnity.

- Non-integrated Pulp Mills

- In May 2004, we sold our non-integrated pulp mills at Brunswick, Georgia, and New Augusta, Mississippi, to Koch Cellulose, LLC and its subsidiaries ("Koch"). In connection with the sale, we agreed to indemnify Koch for certain losses incurred as a result of breaches of certain representations, warranties and covenants made by us contained in the sale agreement. Additionally, we agreed to indemnify Koch for any losses related to pre-closing environmental liabilities. The environmental liability indemnity is subject to a deductible of \$5 million and limited to a cap of \$75 million. The indemnity expires in May 2011. The indemnities related to our representations, warranties and covenants are subject to a deductible of \$2 million and a cap of \$225 million. Most of these indemnities have terms ranging from 18 months to 10 years after the closing date and certain of such indemnities have no expiration date, however we believe exposure to the latter indemnities is limited.

We do not believe that any amounts that we may be required to pay under the indemnities set forth in the agreements relating to the divestitures summarized above will be material to our results of operations, financial position, or liquidity. We will accrue a liability related to a specific indemnity when future payment is probable and the amount is reasonably estimable.



13. **CONDENSED CONSOLIDATING INFORMATION** Fort James is an issuer of certain securities registered under the Securities Act of 1933, thus subjecting it to reporting requirements under Section 15(d) of the Securities Exchange Act of 1934. Fort James guaranteed our \$500 million and \$1.5 billion senior notes offerings (see

Note 10), which were completed on June 3, 2003 and January 30, 2003, respectively. Fort James Operating Company, a subsidiary of Fort James, guarantees the \$500 million senior notes and the securities issued by Fort James. Similarly, certain of our domestic subsidiaries guarantee our Multi-Year Revolving Credit Facility. Each subsidiary issuer or subsidiary guarantor is 100% owned by us and all guarantees are full and unconditional.

Included in Other Non-Guarantor Subsidiaries is our wholly owned subsidiary G-P Receivables, a special purpose entity into which some of our receivables and the receivables of participating domestic subsidiaries are sold. G-P Receivables bought these receivables at a significant discount during the first six months of 2004 resulting in G-P Receivables recognizing a credit to general and administrative expense of \$570 million, and the Corporation, Fort James Guarantor Subsidiary, and Other Non-Guarantor Subsidiaries recognizing a corresponding charge to general and administrative expense of \$512 million, \$5 million and \$53 million, respectively. Prior to December 2003, G-P Receivables purchased the receivables at face value; accordingly, no such income or loss was recognized in the six months of 2003. At the end of the second quarter of 2004, the transfer agreement between G-P Receivables and our participating domestic subsidiaries was amended whereby the discount factor will be substantially reduced for all future purchases. As a result, the general and administrative expenses to be recognized by G-P Receivables will be significantly less in subsequent periods.

Certain assets and liabilities are administered by us, and, accordingly, are maintained at the Corporation and thus are not reflected on the balance sheets of our subsidiaries. The statements of operations properly reflect all results of operations of each respective entity. The following condensed consolidating financial information is presented in lieu of consolidated financial statements for Fort James and Fort James Operating Company because the securities issued by Fort James are fully and unconditionally guaranteed by us:

**CONSOLIDATING STATEMENTS OF INCOME**  
**SECOND QUARTER 2004**

In millions	Georgia-Pacific Corp.	Fort James Corp.	Fort James Guarantor Subsidiary	Fort James Non-Guarantor Subsidiaries	Other Non-Guarantor Subsidiaries	Consolidating Adjustments	Consolidated Amounts
Net sales	\$ 2,867	\$ --	\$ 1,209	\$ 552	\$ 1,145	\$ (585)	\$ 5,188
Costs and expenses	2,257	--	870	406	944	(584)	3,893
Cost of sales	106	--	116	51	31	--	304
Selling and distribution	104	--	63	31	38	--	236

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Depreciation, amortization and accretion	399	--	41	27	(242)	--	225
General and administrative	112	8	96	(62)	24	--	178
Interest, net	(314)	(87)	1	(25)	2	396	(27)
Other (income) losses, including equity income in affiliates							
<b>Total costs and expenses</b>	<b>2,664</b>	<b>(79)</b>	<b>1,187</b>	<b>428</b>	<b>797</b>	<b>(188)</b>	<b>4,809</b>
(Loss) income from continuing operations before income taxes	203	79	22	124	348	(397)	379
(Benefit) provision for income taxes	(32)	(3)	9	50	125	--	149
Income (loss) from continuing operations	235	82	13	74	223	(397)	230
Loss from discontinued operations, net of taxes	(15)	--	--	--	4	1	(10)
<b>Net income (loss)</b>	<b>\$ 220</b>	<b>\$ 82</b>	<b>\$ 13</b>	<b>\$ 74</b>	<b>\$ 227</b>	<b>\$ (396)</b>	<b>\$ 220</b>

CONSOLIDATING STATEMENTS OF INCOME  
SECOND QUARTER 2003

In millions	Georgia-Pacific Corp.	Fort James	Fort James Guarantor Subsidiary	Fort James Non-Guarantor Subsidiaries	Other Non-Guarantor Subsidiaries	Consolidating Adjustments	Consolidated Amounts
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Corp.

Net sales	\$ 2,671	\$ --	\$ 1,228	\$ 534	\$ 1,064	\$ (614)	\$ 4,883
Costs and expenses	2,306	--	894	378	883	(614)	3,847
Cost of sales	127	--	118	49	27	--	321
Selling and distribution	112	--	64	28	39	--	243
Depreciation, amortization and accretion	112	--	40	40	15	--	207
General and administrative	128	3	104	(58)	25	--	202
Interest, net	(145)	(69)	1	--	2	195	(16)
Other losses (income), including equity income in affiliates							
Total costs and expenses	2,640	(66)	1,221	437	991	(419)	4,804
(Loss) income from continuing operations before income taxes	31	66	7	97	73	(195)	79
(Benefit) provision for income taxes	(41)	(1)	4	31	32	--	25
Income (loss) from continuing operations	72	67	3	66	41	(195)	54
(Loss) income from discontinued operations, net of taxes	(11)	--	--	--	18	--	7
Net (loss) income	\$ 61	\$ 67	\$ 3	\$ 66	\$ 59	\$ (195)	61

CONSOLIDATING STATEMENTS OF INCOME  
FIRST SIX MONTHS 2004

In millions	Georgia-Pacific Corp.	Fort James Corp.	Fort James Guarantor Subsidiary	Fort James Non-Guarantor Subsidiaries	Other Non-Guarantor Subsidiaries	Consolidating Adjustments	Consolidated Amounts
Net sales	\$ 5,888	\$ --	\$ 2,350	\$ 1,130	\$ 2,229	\$ (1,187)	\$ 10,410
Costs and expenses	4,698	--	1,688	799	1,860	(1,187)	7,858
Cost of sales	265	--	241	97	59	--	662
Selling and distribution	216	--	124	67	73	--	480
Depreciation, amortization and accretion	791	--	84	57	(488)	--	444
General and administrative	243	17	192	(123)	46	--	375
Interest, net	(591)	(183)	2	(26)	3	794	(1)
Other (income) losses, including equity income in affiliates							
Total costs and expenses	5,622	(166)	2,331	871	1,553	(393)	9,818