

KAPSTONE PAPER & PACKAGING CORP
Form 10-K
March 31, 2009

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**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549**

FORM 10-K

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

For the fiscal year ended December 31, 2008

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

For the transition period from _____ to _____
Commission File No.: 001-33494

KapStone Paper and Packaging Corporation

(Exact Name of Registrant as Specified in its Charter)

Delaware
(State or other jurisdiction of
Incorporation or organization)

20-2699372
(I.R.S. Employer
Identification No.)

**KapStone Paper and Packaging Corporation
1101 Skokie Blvd. Suite 300
Northbrook, IL 60062**

(Address of Principal Executive Offices) (ZIP Code)

Registrant's telephone number, including area code: **(847) 239-8800**

SECURITIES REGISTERED PURSUANT TO SECTION 12(B) OF THE ACT:

Title of Each Class	Name of Exchange On Which Registered
Common Stock (Par Value \$.0001)	Nasdaq Stock Market, LLC
Warrants to purchase Common Stock	Nasdaq Stock Market, LLC

SECURITIES REGISTERED PURSUANT TO SECTION 12(G) OF THE ACT: **NONE**

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been

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subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of the registrant's knowledge in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definition of the above in Rule 12b-2 of the Exchange Act.

Large Accelerated Filer <input type="checkbox"/>	Accelerated Filer <input checked="" type="checkbox"/>	Non-Accelerated Filer <input type="checkbox"/>	Smaller Reporting Company <input type="checkbox"/>
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Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

The aggregate market value of the 18,172,973 shares of Common Stock held by non-affiliates of the registrant on June 30, 2008 was \$121,213,730. This calculation was made using a price per share of Common Stock of \$6.67, the closing price of the Common Stock on the NASDAQ on June 30, 2008, the last day of the registrant's most recently completed second fiscal quarter of 2008. Solely for purposes of this calculation, all shares held by directors and executive officers of the registrant have been excluded. This exclusion should not be deemed an admission that these individuals are affiliates of the registrant.

On February 28, 2009, the number of shares of Common Stock outstanding, excluding 40,000 treasury shares, was 28,370,248.

DOCUMENTS INCORPORATED BY REFERENCE:

The registrant's Definitive Proxy Statement for its 2009 Annual Meeting of Stockholders will be filed with the Securities and Exchange Commission no later than 120 days after the end of the fiscal year covered by this Form 10-K pursuant to General Instruction G(3) of the Form 10-K. Information from such Definitive Proxy Statement will be incorporated by reference into Part III, Items 10, 11, 12, 13 and 14 hereof.

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Forward Looking Statements.

This Annual Report on Form 10-K includes forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. We have based these forward-looking statements on our current expectations and projections about future events. These forward-looking statements are subject to known and unknown risks, uncertainties and assumptions about us, including the risks set forth in Item 1A. Risk Factors below, that may cause our actual results, levels of activity, performance or achievements to be materially different from any future results, levels of activity, performance or achievements expressed or implied by such forward-looking statements. In some cases, you can identify forward-looking statements by terminology such as "may," "should," "could," "would," "expect," "plan," "anticipate," "believe," "estimate," "continue," or the negative of such terms or other similar expressions. Factors that might cause or contribute to such a discrepancy include, but are not limited to, those described in our other Securities and Exchange Commission filings. All subsequent written and oral forward-looking statements attributable to KapStone or persons acting on our behalf are expressly qualified in their entirety by the cautionary statements in this paragraph. KapStone disclaims any intention or obligation to publicly announce the results of any revisions to any of the forward-looking statements contained herein to reflect future events or developments.

PART I

Item 1. Business

Overview

KapStone Paper and Packaging Corporation, formerly Stone Arcade Acquisition Corporation, ("KapStone" or the "Company") was formed in Delaware as a special purpose acquisition corporation on April 15, 2005 for the purpose of effecting a merger, capital stock exchange, asset acquisition or other similar business combination with an unidentified operating business in the paper, packaging, forest products and related industries.

On August 19, 2005, we consummated our initial public offering of 20,000,000 units with each unit consisting of one share of our common stock and two warrants. Each warrant entitles the holder to purchase one share of our common stock at an exercise price of \$5.00 per share. The units sold in our initial public offering were sold at an offering price of \$6.00 per unit, generating gross proceeds of \$120.0 million.

On January 2, 2007, we consummated the purchase from International Paper Company ("IP") of substantially all of the assets, and the assumption of certain liabilities, of the Kraft Papers Business ("KPB") for \$155 million subject to certain adjustments. The assets consisted of an unbleached kraft paper manufacturing facility in Roanoke Rapids, North Carolina, and Ride Rite® Converting, an inflatable dunnage bag manufacturer located in Fordyce, Arkansas, trade accounts receivable and inventories. The liabilities assumed consisted of trade accounts payable, accrued expenses and certain long-term liabilities. The purchase price included two contingent earn-out payments of up to \$60 million if certain EBITDA targets are achieved. We obtained a \$95 million senior secured credit facility from LaSalle Bank National Association, which was used to fund a portion of the KPB purchase price.

On July 1, 2008, we consummated the purchase from MeadWestvaco Corporation ("MWV") of substantially all of the assets and the assumption of certain liabilities of the Charleston Kraft Division ("CKD"), for \$485 million, subject to certain adjustments. The assets consisted of an unbleached kraft paper manufacturing facility in North Charleston, South Carolina, including a cogeneration facility, chip mills located in Elgin, Hampton, Andrews and Kinards, South Carolina and a lumber mill located in Summerville, South Carolina, trade accounts receivables and inventories. The liabilities assumed consisted of trade accounts payable, accrued expenses and certain long-term liabilities.

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The CKD acquisition was financed by cash on hand and by a new senior secured credit facility of \$515 million consisting of a five-year term loan of \$390 million, a seven-year term loan of \$25 million and a \$100 million revolving credit facility. In addition, \$40 million of seven-year 8.30% senior notes were issued. As part of the transaction the Company paid off the remaining amount due under its prior credit facility.

The CKD business was deemed an attractive acquisition candidate based upon meeting the Company's objectives of being a North American-based, profitable company in the paper and packaging industry and for its synergies with the Company's existing operations.

Acquisitions

We intend to pursue other acquisition opportunities in an effort to diversify and/or grow our business. We have been and continue to be engaged in evaluating a number of potential acquisition opportunities and have had preliminary discussions with several potential targets. No assurance can be given that we will consummate additional transactions. The structuring and financing of any future acquisitions may be dependent on the terms and availability of additional financing to us that either replaces or does not conflict with the Company's existing senior secured credit facility.

General

We produce and sell a variety of unbleached kraft paper, linerboard, folding carton board, saturating kraft, inflatable dunnage bags and dimensional lumber. We review our business based on the following operating segments: unbleached kraft, dunnage bags and lumber.

In 2008, following completion of the CKD acquisition, the Company determined, in accordance with Statement of Financial Accounting No. 131, *Disclosures about Segments of an Enterprise and Related Information*, to make changes to its reportable segments. All segment disclosures in this Report are presented in conformance with the new presentation. For additional information regarding the change in segments, and the results of our segments, please see Note 16 of the Notes to Consolidated Financial Statements.

Industry Overview

Unbleached kraft paper market

We view the unbleached kraft paper market as including unbleached kraft paper, linerboard, saturating kraft and unbleached folding carton stock.

American Forest and Paper Association ("AF&PA") estimates that the size of the U.S. unbleached kraft paper market was approximately 1.56 million tons in 2008 up slightly from 1.55 million tons in 2007. The U.S. produced 1.49 million tons in 2008 compared to 1.36 million tons in 2007. In 2008, 0.25 million tons were imported and 0.18 million tons were exported. In 2007, 0.36 million tons were imported and 0.17 million tons were exported. U.S. operating rates for 2008 and 2007 were approximately 93% and 94%, respectively, based on the AF&PA's 48th Annual Capacity Survey. The kraft paper market is comprised of three general product types: (1) Multiwall; (2) Specialty converting (including rollwrap); and (3) Grocery bag and sack.

Both the multiwall packaging markets and the grocery bag and sack markets contracted between 2001 and 2008. The multiwall market contracted due to conversion to plastics in certain end-use markets (primarily in the insulation and lawn and garden markets) as well as the transition to 2-ply extensible sack packaging in certain markets (primarily in the cement market) where the package was considered a large percentage in the overall cost of the total product.

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In 2007, the Department of Commerce announced antidumping duties to be imposed on imports of laminated woven sacks from China. The duties will be an important first step for Paper Shipping Sack Manufacturers' Association, Inc. ("PSSMA") members in regaining market share.

Linerboard is primarily used to manufacture corrugated containers for packaging products. U.S. demand for corrugated boxes and linerboard tends to be driven by industrial production of processed foods, nondurable goods as well as certain durable goods. AF&PA reported that 2008 linerboard production of approximately 24.2 million tons was down from 25.2 million tons in 2007 resulting in a reduction in capacity utilization of 6.2% to 91%. We target our linerboard for specialty independent corrugated and laminated products customers who focus on specialty niche packaging.

Saturating kraft is a worldwide market of approximately 850,000 tons in 2008. It is a specialty product where the three major manufacturers (KapStone, International Paper, and Stora Enso) produce approximately 75% of the world's requirement. The remainder is supplied by local producers of lower quality material in various regions of the world. There are no published statistics for this grade. KapStone, through internal research believes that growth rates for the grade are greater than 3% per year for China, India, Southeast Asia, Latin America and portions of Europe. The overall market from 2007 through 2008 is flat due to declines in North America and the majority of Western Europe. Demand is affected by construction, remodeling activity, electronics manufacturing, and furniture manufacturing in the various regions of the world. Barriers to entry for producing high quality saturating kraft are high as it is a technically difficult grade to produce.

Unbleached, uncoated folding carton stock is a North American market of approximately 350,000 tons of production in 2008. The Company's Kraftpak® product is a unique low density, virgin fiber grade competing in this market with uncoated recycled board ("URB"). Major URB producers include Newark, Rock Tenn and Caraustar. KapStone believes that total unbleached folding carton production in North America was approximately flat in 2008 compared to 2007. Kraftpak® has also successfully found applications for consumer brands that are changing their image to promote environmental friendliness and sustainability. KapStone believes that these are the best growth opportunities for Kraftpak® in that they take share from Coated Recycled Board, Coated Natural Kraft Board, and Solid Bleached Sulfate Board, which are much larger markets.

Dunnage bags market

The demand for dunnage bags, which are used to protect products during transportation, is correlated to the general freight transportation industry. The American Trucking Association ("ATA") estimates that nearly 70% of U.S. freight volume, which includes general and bulk freight, is transported by trucks.

Lumber market

Lumber is a commodity business tied closely to housing starts and remodeling activity. Weak activity in the housing market in 2007 and 2008 has negatively impacted both volume and pricing. The Company's lumber mill in Summerville is an efficient, high quality producer with a focus on excellent service to local lumber retailers and treating companies in order to maximize profitability.

Customers

Unbleached kraft

The unbleached kraft segment has over 400 customers, many of which are leading world class converters of kraft paper. In 2007 the unbleached kraft segment had approximately 100 customers. Upon acquiring CKD in July of 2008, the unbleached kraft segment had approximately 400 customers of which approximately 100 were based in foreign countries. The segment's top three customers

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accounted for approximately \$118.0 million, \$92.9 million and \$100.4 million of consolidated net sales in 2008, 2007 and 2006, or approximately 24.3%, 40.8% and 46.9% of all unbleached kraft revenues generated in 2008, 2007 and 2006, respectively. Graphic Packaging accounted for 10.7% of consolidated net sales in 2008. Altivity Packaging Corporation and Exopack, LLC, accounted for 17.1% and 10.4% of consolidated net sales in 2007, respectively, and 20.3% and 11.1% of consolidated net sales in 2006, respectively. In 2008, Graphic Packaging acquired Altivity Packaging Corporation. Kapstone continues to build long-term relationships, most of which were established by KPB as a division of IP and CKD as a division of MWV. We believe that the risk of losing customers or business with customers is reduced due to the long-term relationships that have been established.

Linerboard is sold to converters in the corrugated box industry and to other converters for a variety of end uses including laminated tier sheets for the bottling industry and wrapping material, among others. The focus is on independent producers who do not have their own mill systems or producers who commonly purchase liner on the open market.

Our Saturating Kraft customer base is evenly split between three geographic regions, the Americas, Europe and Asia. Approximately 70% of our sales are exports to customers in Europe, Latin America and Asia where growth opportunities are favorable. KapStone or its Predecessor have done business with many of these customers for well over 30 years. Some customers have consolidated to form a greater presence in their markets. Customer consolidation is particularly evident for North America and just in the beginning phase in Europe. In Asia, there are numerous players and it is a highly fragmented market making it difficult entry for some companies that do not have a presence in the region.

Our major customers' end-use markets are in the thin high pressure laminates (HPL) creating decorative surfaces such as kitchen and bath countertops, home and office furniture and flooring. In Europe, there is a growing and distinct HPL segment that involves a much thicker product called Compact laminates, which create surfacing products such as exterior cladding, partitions and doors. In Asia, there is significant use of our products for the manufacturing of Printed Circuit Boards (PCB) and Copper Clad Laminates (CCL) and there is also a growing use for thin HPL in Decorative surfaces. KapStone has acquired a leadership position through knowledge of our markets and understanding the technical needs of our customers' manufacturing process and the demanding requirements of their products.

Dunnage bags

The dunnage bags segment sold under the Ride Rite® Converting brand has a customer base consisting of leading distributors of shipping and packing materials, manufacturers, less-than-truckload carriers and retail regional distribution centers. No customer in the dunnage bag segment accounted for more than 10% of consolidated net sales for the years 2008, 2007 and 2006. The segment's top ten customers accounted for \$20.9 million of net sales in 2008, \$20.3 million of net sales in 2007 and \$23.2 million of net sales in 2006, representing 63%, 62% and 65% of Ride Rite® Converting's net sales in 2008, 2007 and 2006, respectively. In connection with the KPB acquisition, IP entered into an agreement to continue purchasing dunnage bags from Ride Rite® Converting for a period of five years.

In February 2008, Sunrise Arkansas, a large customer in our dunnage bag segment, was purchased by Illinois Tool Works ("ITW"). ITW also owns Shippers Products Inc., which manufactures dunnage bags and competes directly with Ride Rite® Converting.

Lumber

Our lumber business sells approximately 58% of its lumber to third parties who apply preservatives to the product and resell it for exterior applications. Approximately 18% is sold for industrial applications, 14% to wholesalers, 7% to retail stores and 3% for engineered wood applications. The

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lumber business has approximately 95 customers. Approximately 47% of revenues is under contracts which are generally a year in length. No customer in the lumber segment accounted for more than 10% of consolidated net sales for the year ended December 31, 2008.

Sales and Marketing

The sales and marketing team works directly with our technical, manufacturing and product development teams to offer solutions and meet new customer demands and product requirements. We market and sell our products through a national sales force for our domestic unbleached kraft business. Our international unbleached kraft business is supported by sales teams based in Europe and Asia. We sell export linerboard to unaffiliated resellers. Our dunnage bag and lumber businesses are supported by their own dedicated sales force.

Manufacturing and Distribution

Unbleached kraft

Our unbleached kraft paper and board manufacturing facilities are based in Roanoke Rapids, North Carolina and North Charleston, South Carolina and includes production facilities consisting of integrated pulp and paper mills that produce unbleached kraft paper, linerboard, saturating kraft products sold under the DuraSorb® brand and folding carton board sold under the Kraftpak® brand. Our Roanoke Rapids paper mill began operations in 1907 and North Charleston paper mill began operations in 1937.

The Company's paper mills' annual production capacity is approximately 1.3 million tons. The Company offers a portfolio of product grades, which are sold to customers who convert them into a wide range of products. The kraft paper is primarily used to produce multiwall bags for agricultural products, pet food, cement and chemicals, grocery bags and specialty conversion products such as wrapping paper products, dunnage bags and rollwrap. The linerboard grades are primarily used to produce manufacturing corrugated containers for packaging products. DuraSorb® saturating kraft is primarily used to manufacture decorative laminates used in home and office furniture products and industrial laminates and overlays used in electronics and construction applications. Kraftpak® folding carton board is an unbleached board used in the manufacture of folding cartons.

The Company's facilities are in good operating condition and are suited for the purpose for which they are presently being used. Machinery and equipment is regularly inspected to maintain good working order through annual planned maintenance outages.

Softwood pulp used to make unbleached kraft paper, folding carton board and linerboard is produced from a combination of locally sourced roundwood and pine woodchips. After the wood is debarked and chipped, the chips are loaded into digesters for cooking. Woodchips, chemicals and steam are mixed in the digester to produce softwood pulp. Hardwood pulp is produced in North Charleston in a similar fashion for the production of DuraSorb® saturating kraft. The pulp is screened and washed through a series of washers, and then stored prior to the paper making process. The Company processes softwood pulp using up to five unbleached kraft paper machines. Management monitors productivity on a real-time basis with on-line reporting tools that track production values versus targets. Overall equipment efficiency is also monitored daily through production reporting systems.

The majority of our domestic sales are distributed directly to customers who convert the paper into end-market finished products. Export linerboard paper is sold primarily to third party resellers.

Dunnage bags

Our dunnage bag business, based in Fordyce, Arkansas, produces and sells inflatable paper dunnage bags under the Ride Rite® Converting trademark. The bags are constructed of an internal

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poly liner encased by multiple layers of high strength unbleached kraft paper and/or linerboard and are used to secure freight to minimize movement and potential damage of goods and products during transport. Ride Rite® Converting uses unbleached kraft paper produced by the unbleached kraft segment for approximately two-thirds of its requirements. Additionally, the bags have an optional reusable valve design, which allows for the inflation and deflation of the bags for multiple uses. Ride Rite® Converting produces over 230 varieties of its inflatable dunnage bags. Ride Rite® Converting products are sold to manufacturers, less-than-trailer-load distributors, and retail regional distribution centers.

Lumber

Our Summerville lumber mill produces approximately 95 million board feet per year of kiln dried, southern pine lumber in many dimensions. Significant amounts of its products in decking, timbers and dimension lumber of various grades are sold to customers who apply preservatives to the lumber and resell it for exterior applications. Other customers purchase lumber for the manufacture of engineered wood trusses and resale through local or national brand building supply stores or for various industrial uses in the packaging and pallet industries. The lumber mill produces residual softwood chips from sawmilling as well as chips from a pulpwood chipping operation to supply the North Charleston paper mill.

Transitional Support

We have entered into two transitional services agreements to provide for certain services, including information technology and centralized transaction processing, until we could convert acquisitions to our own ERP systems. The term of each of the services ranges from six months to approximately 18 months, but our goal is to terminate all of the services promptly in order to reduce costs. Our transitional support services from IP ended in April 2008. Our transitional service agreement with MWV, which began on July 1, 2008, is projected to continue throughout 2009. The total cost of transferring services from IP to us was approximately \$6.0 million, consisting primarily of the cost of installing a new enterprise resource planning system which included general ledger, order entry and receivables management, purchasing and payment plus additional modules. The system supports operations in North Carolina and Arkansas as well as the corporate headquarters. The transitional services being provided by MWV is estimated at approximately \$9.0 million in total from July 1, 2008 through the third quarter of 2009. We expect to incur approximately \$8.0 million to migrate and upgrade the Charleston operations to our Enterprise Resource Planning System ("ERP").

Suppliers

Unbleached kraft

The raw materials needed to process unbleached kraft paper and related products consists primarily of roundwood, woodchips and chemicals. In addition, we purchase coal, fuel oil and natural gas to run boilers and our cogeneration facility in South Carolina. We believe that these raw materials are readily available and that there are a number of suppliers from whom the materials can be bought in the open market.

In 2008 approximately 20% of our combined paper mills' fiber supply (roundwood and woodchips) was delivered under long-term supply agreements. Upon acquisition of the CDK business from MWV, we entered into a 15 year fiber supply agreement whereby MWV provides us with up to 25% of our South Carolina fiber requirements with prices tied to a market index. The balance of fiber is purchased from third parties in North Carolina, Virginia, Georgia and South Carolina.

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The primary chemical used in our pulp making process is caustic soda and is purchased at market prices. We have fixed-pricing contracts with two long-term suppliers for coal. Fuel oil is purchased from third parties at market prices.

Typical contracts for raw materials range from one to three years in length and are at fixed pricing or tied to a documented moving index for each material. As costs for raw materials, supplies and services increase, we implement price increases to recover these rising material costs from our customers, when possible. We currently do not use futures contracts or enter into hedging arrangements to manage the risk of fluctuations in coal or fuel prices. Thus, if we cannot pass on the rise in energy or other costs to our customers, such rise in costs will have an adverse effect on our gross profit margins.

Dunnage bags

Ride Rite® Converting purchases approximately two-thirds of its kraft paper requirements from KapStone's unbleached kraft operating segment. Other key materials such as resin and valves are purchased from a combination of domestic and foreign suppliers.

Lumber

Approximately 60% of the saw timber used in lumber production is supplied by MWV under the terms of a 15 year fiber supply agreement. The remaining saw timber is sourced from other third parties.

Competition

Unbleached kraft

We are one of the leading manufacturers of unbleached kraft paper in North America. Other key U.S. market suppliers are Georgia-Pacific Corporation, Longview Fibre, Delta Natural, and Smurfit Stone. A number of other competitors comprise the remainder of North American unbleached kraft paper production.

We believe the key parameters on which North American unbleached kraft suppliers compete are supply reliability, delivered price and product quality. KPB and now Kapstone have longstanding relationships with many of their customers and historically have entered into contracts with initial terms of at least two years. We believe our longstanding relationships are based on our ability to provide the best value proposition to our customers through quality products, consistent and reliable service and technical innovation.

The overall U.S. linerboard capacity is in excess of 25 million tons. As such the market share between our two mills is just over two percent. International Paper is the largest producer, followed by Smurfit-Stone Container, Georgia-Pacific and Temple-Inland Packaging Corporation. Our emphasis is on the independent producers of corrugated packaging and other users of linerboard. The products we produce are included in the grouping known as Kraft liner which is considered a premium product of the linerboard market.

Dunnage bags

We believe that two companies that account for over 50% of the North American paper inflatable dunnage bag market: Ride Rite® Converting and Shippers Products Inc., a division of ITW.

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Lumber

Competition for our lumber business includes large multisite companies such as New South, West Fraser, International Paper and Georgia Pacific, as well as smaller local sawmills.

Environmental Regulation

Our operations are subject to environmental regulation by federal, state, and local authorities in the United States, including requirements that regulate discharge into the environment, waste management, and remediation of environmental contamination. Environmental permits are required for the operation of our businesses and are subject to revocation, modification and renewal. Governmental authorities have the power to enforce compliance with environmental requirements and violators are subject to injunctions, civil penalties and criminal fines. Third parties may also have the right to sue to enforce compliance with such regulations.

KapStone is committed to maintaining high environmental quality standards which meet or exceed those established by all relevant environmental laws, regulations and other applicable requirements including Sustainable Forestry Initiatives. KapStone's goal is 100% compliance with all environmental laws and regulations wherever we do business. This is achieved by identifying, understanding and giving priority consideration to the environmental aspects and impacts of KapStone's activities, products and services while integrating continual environmental improvement, pollution prevention and employee diligence into daily operations.

On September 13, 2004, EPA published the Boiler MACT regulations affecting industrial boilers and process heaters burning all fuel types with the exception of small gas-fired units. On July 30, 2007, the U.S. Court of Appeals for the D.C. Circuit remanded and vacated the Boiler MACT. We continue to monitor the process the EPA is undertaking to develop new standards for industrial boilers and process heaters so that we can determine our liability regarding any future related regulations.

On July 30, 2004, EPA published the Plywood and Composite Wood Panel (or PCWP) MACT standards. Our Summerville lumber mill is in compliance with PCWP MACT which required compliance by October 1, 2008.

The EPA is continuing the development of new programs and standards such as additional wastewater discharge allocations, water intake structure requirements and national ambient air quality standards. We believe that our operations are in compliance in all material respects with all current environmental regulations and are not aware of any pending regulatory agency compliance actions.

The U.S. Congress is actively considering legislation to reduce emissions of greenhouse gases. In addition, several states have already taken legal measures to require the reduction of emissions of greenhouse gases by companies and public utilities, primarily through the planned development of greenhouse gas emission inventories and/or regional greenhouse gas cap and trade programs. Passage of climate control legislation by Congress or various states of the U.S., or the adoption of regulations by the Environmental Protection Agency or analogous state agencies that restrict emissions of greenhouse gases in areas in which we conduct business, may have a material effect on our operations in the United States. We expect that we will not be disproportionately impacted by these measures as compared to typical owners of comparable properties in the United States.

Employees

At December 31, 2008, KapStone had approximately 1,750 employees. Of these employees, approximately 1,100 employees were covered by collective bargaining agreements with the United Steel Workers. Currently, there are collective bargaining agreements in place with union employees in Roanoke Rapids, North Carolina, through August 31, 2010, in North Charleston, South Carolina

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through June 30, 2009 and with Ride Rite® Converting through June 30, 2011. We believe that we have a good relationship with our employees and union leadership.

In January 2007, upon consummation of the acquisition of KPB, we began hiring a corporate staff to manage our operations. This included a vice president and chief financial officer, a vice president and general manager to manage KPB and other corporate staff employees. Additional hiring at the corporate headquarters occurred throughout 2007 and 2008.

As part of the CKD acquisition, we acquired 11 employees who are located in Europe and Asia. These employees perform sales and order entry activities in support of the Company's export shipments to customers based in Europe and Asia.

International Sales

For the years ended December 31, 2008 and 2007 the Company had export shipments from the United States to customers in foreign countries of \$165 million and \$44 million, respectively. No foreign country accounted for more than 10% of consolidated net sales for either year.

Executive Officers of Registrant

Our executive officers are as follows:

Name	Age	Position
Roger W. Stone	74	Chairman of the Board and Chief Executive Officer
Matthew Kaplan	52	President and Secretary
Andrea K. Tarbox	58	Vice President and Chief Financial Officer
Timothy P. Keneally	61	Vice President and General Manager

Roger W. Stone has been Chairman of the Board and Chief Executive Officer since our inception. Mr. Stone was Manager of Stone-Kaplan Investments, LLC, a private investment company, from July 2004 through December 2007. He was Chairman and Chief Executive Officer of Box USA Holdings, Inc., a corrugated box manufacturer, from July 2000 until the sale of that company in July 2004. Mr. Stone was Chairman, President and Chief Executive Officer of Stone Container Corporation, a multinational paper company primarily producing and selling pulp, paper and packaging products, from March 1987 to November 1998 when Stone Container Corporation merged with Jefferson Smurfit Corporation, at which time he became President and Chief Executive Officer of Smurfit-Stone Container Corporation until March 1999. Mr. Stone has served on the board of directors of McDonald's Corporation since 1989. Mr. Stone received a B.S. in Economics from the Wharton School at the University of Pennsylvania. Mr. Stone is the father-in-law of Matthew Kaplan.

Matthew Kaplan has been our President and Secretary since our inception. Mr. Kaplan was Manager of Stone-Kaplan Investments, LLC, a private investment company, from July 2004 through December 2007. He was President, Chief Operating Officer and a director of Box USA Holdings, Inc., a corrugated box manufacturer, from July 2000 until the sale of the company in July 2004. Mr. Kaplan began his career at Stone Container Corporation in 1979 and was serving as its Senior Vice President and General Manager of North American Operations when Stone Container Corporation merged with Jefferson Smurfit Corporation in November 1998. He was Vice President/General Manager, Container Division with Smurfit-Stone Container Corporation until March 1999. Mr. Kaplan has served on the board of advisors of Victory Packaging since January 2007. In addition, Mr. Kaplan has also served on the board of trustees of Magnetar Spectrum Fund since November 2007. Mr. Kaplan received a B.A. from the Wharton School in Economics from the University of Pennsylvania and an M.B.A. from the University of Chicago. Mr. Kaplan is the son-in-law of Roger W. Stone.

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Andrea K. Tarbox was appointed Vice President and Chief Financial Officer in January 2007. Ms. Tarbox served as a financial consultant to the Company from April 2006 until her appointment as Vice President and Chief Financial Officer. Ms. Tarbox played a key financial role in the acquisition by the Company of the Kraft Papers Business from International Paper Company. From March 2003 through March 2006, Ms. Tarbox served as Chief Financial and Administrative Officer for Uniscribe Professional Services, Inc. From July 1994 until February 2003, Ms. Tarbox was employed by Gartner Inc., last serving as Group Vice President-Finance and Treasurer. Prior to that, Ms. Tarbox had assumed financial positions of increasing responsibility in several global companies including British Petroleum, p.l.c. and Fortune Brands, Inc. Ms. Tarbox began her career with Ernst & Young LLP and is a Certified Public Accountant. Ms. Tarbox earned a B.A. degree in Psychology from Connecticut College and an M.B.A. from the University of Rhode Island.

Timothy P. Keneally has been our Vice President and General Manager of the kraft paper business since its acquisition from International Paper in January 2007. Previously, Mr. Keneally led the International Paper team that assessed the review of strategic alternatives relating to the kraft paper business. He was the lead person in presenting the historical performance of the business and assisted in defining the future strategy for the business. Mr. Keneally has 35 years of experience in the paper and packaging industry. Mr. Keneally earned a B.A. degree in History from Marist College in Poughkeepsie, NY.

Website Access to Company Reports

The Company's annual reports on Form 10-K, including this Form 10-K, as well as the quarterly reports on Form 10-Q and current reports on Form 8-K, and all amendments to those reports are filed electronically with the Securities and Exchange Commission ("SEC") and are also available free of charge through our website, www.kapstonepaper.com as soon as reasonably practicable after such material is filed electronically with, or furnished to, the SEC. Also, copies of our annual report will be made available, free of charge, upon written request.

Item 1A Risk Factors

You should carefully consider the following risk factors, together with the other information contained in this annual report on Form 10-K, in evaluating us and our business before making an investment decision regarding our securities. If any of the events or circumstances described in the following risk factors were to actually occur, our business, financial condition or results of operations could be materially and adversely affected. The risks listed below are not the only risks that we face.

Risks associated with our business

Recent changes in U.S. and global economic conditions could have a continuing adverse effect on the profitability of some or all of our businesses.

Recent concerns over declining consumer and business confidence, the availability and cost of credit, reduced consumer spending and business investment, the volatility and strength of the capital and credit markets, and inflation all affect the business and economic environment and, ultimately, the profitability of our business. In an economic downturn characterized by higher unemployment, lower family income, lower corporate earnings, lower business investment and lower consumer spending, the demand for our products is adversely affected. Adverse changes in the economy could negatively affect earnings and could have a material adverse effect on our business, results of operations, cash flows and financial position. We cannot predict whether or when such circumstances may occur, or what impact, if any such circumstances could have on our business, results of operations, cash flows and financial position.

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Conditions in the global capital and credit markets and the economy generally may materially adversely affect our business, results of operations and financial position and we do not expect these conditions to improve in the near future.

Our results of operations and financial position could be materially affected by adverse changes in the global capital and credit markets and the economy generally, including recent declines in consumer and business confidence and spending, both in the U.S. and elsewhere around the world. The capital and credit markets have been experiencing extreme volatility and disruption in recent months. In some cases, these markets have exerted downward pressure on availability of liquidity and credit and increased the costs of credit when such credit is available. Conditions in the capital and credit markets and the effects of the declines in consumer and business confidence and spending may adversely impact the ability of our lenders, suppliers and customers to conduct their business activities. The consequences of such adverse effects could include the interruption of production at the facilities of our customers, the reduction, delay or cancellation of customer orders, delays in or the inability of customers to obtain financing to purchase our products, and bankruptcy of customers or other creditors. Moreover, the current worldwide financial crisis has reduced the availability of liquidity and credit to fund or support the continuation and expansion of business operations worldwide as many lenders and institutional investors have reduced and, in some cases, ceased to provide funding to borrowers.

While we have procedures to monitor and limit exposure to credit risk, there can be no assurance such procedures will effectively limit our credit risk and avoid losses, which could have a material adverse effect on our financial condition and operating results.

We rely on key customers.

During the year ended December 31, 2008, our largest customer, Graphic Packaging, accounted for approximately 10.7% of consolidated net sales. This customer is in the unbleached kraft operating segment. A loss of this customer or other key customers could significantly impact our financial results.

We are dependent upon key management executives whose loss may adversely impact our business.

Our success depends significantly on the efforts and abilities of Roger W. Stone, Chairman of the Board and Chief Executive Officer, and Matthew Kaplan, President. The loss of services of one or both of these individuals could have a material adverse effect on our business.

In addition, we depend on the expertise, experience and continued services of KPB's and CKD's management. The loss of such management, or an inability to attract or retain other key individuals, could materially adversely affect us. We seek to compensate management, as well as other employees, through competitive salaries, bonuses and other incentive plans, but there can be no assurance that these programs will allow us to retain key management executives or hire new key employees.

KapStone's substantial indebtedness may adversely affect its financial health.

As of December 31, 2008, KapStone had an aggregate principal amount of approximately \$440 million of outstanding debt. As a result of the indebtedness, KapStone's ability to obtain additional financing for working capital, capital expenditures, acquisitions or other general corporate purposes may be impaired in the future. The substantial debt could make us vulnerable to economic downturns and may hinder our ability to adjust to rapidly changing market conditions.

A substantial portion of our cash flow from operations will be needed to meet the payment of principal and interest on our indebtedness. The business may not generate sufficient cash flow from operations to enable it to repay KapStone's indebtedness and to fund other liquidity needs, including capital expenditure requirements. The indebtedness incurred by KapStone under its senior secured

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credit facility bears interest at variable rates, and therefore if interest rates increase, KapStone's debt service requirements will increase. In such case, KapStone may need to refinance or restructure all or a portion of its indebtedness on or before maturity. KapStone may not be able to refinance any of its indebtedness, including the senior secured credit facility, on commercially reasonable terms, or at all. If KapStone cannot service or refinance its indebtedness, it may have to take actions such as selling assets, seeking additional equity or reducing or delaying capital expenditures, any of which could have a material adverse effect on our operations and financial condition.

KapStone's senior secured credit facility contains restrictive covenants that limit its liquidity and corporate activities. KapStone's credit facility imposes operating and financial restrictions that limit KapStone's ability to:

incur additional indebtedness;

create additional liens on its assets;

make investments;

engage in mergers or acquisitions;

pay dividends; and

sell all or any substantial part of assets

In addition, the credit facility also imposes other restrictions on KapStone. Therefore, we will need to seek permission from the lenders in order to engage in certain corporate actions. The lender's interests may be different from ours, and no assurance can be given that we will be able to obtain the lender's permission when needed. This may prevent us from taking actions that are in our best interest.

The credit facility requires KapStone to maintain certain financial ratios. The failure to maintain the specified ratios could result in an event of default if not cured or waived.

In the event of a default under KapStone's senior credit facility, the lenders generally would be able to declare all of such indebtedness, together with accrued interest, to be due and payable. In addition, borrowings under the credit facility are secured by a first priority lien on all assets of the Company and, in the event of a default under that facility the lenders generally would be entitled to seize the collateral. A default under any debt instrument, unless cured or waived, would likely have a material adverse effect on our business and financial condition.

If we fail to extend or renegotiate the collective bargaining agreements with the United Steelworkers Union as they expire from time to time, or if our unionized employees were to engage in a strike or other work stoppage, our business and operating results could be materially harmed.

Most of our hourly paid employees are represented by trade unions. The Company is a party to collective bargaining contracts which represent approximately 615 employees at the North Charleston locations, 381 employees at Roanoke Rapids and 136 employees at Ride Rite® Converting. No assurance can be given that we will be able to successfully extend or renegotiate the collective bargaining agreements as they expire from time to time. Currently, there are collective bargaining agreements in effect with respect to North Charleston through June 30, 2009, Roanoke Rapids through August 31, 2010, and with respect to Ride Rite® Converting through June 30, 2011. If we are unable to extend or negotiate new agreements without work stoppages, it could negatively impact our ability to manufacture our products and adversely affect results of operations.

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As a result of the CKD acquisition, our operations have become increasingly global in nature. Our business, financial condition and results of operations could be adversely affected by the political and economic conditions of the countries in which we conduct business, by fluctuations in exchange rates and other factors related to our international operations.

Approximately 32% of our annual revenues in 2008 were derived from export sales. As our international operations and activities expand, we face increasing exposure to the risks of selling to customers in foreign countries. These factors include:

Changes in foreign currency exchange rates which could adversely affect our competitive position, selling prices, and therefore the demand for our products in a particular market.

Trade protection measures in favor of local producers of competing products, including government subsidies, tax benefits, trade actions (such as anti-dumping proceedings) and other measures giving local producers a competitive advantage over the company.

Changes generally in political, regulatory or economic conditions in the countries in which we conduct business.

These risks could affect the cost of selling our products, our pricing, sales volume, and ultimately our financial performance. The likelihood of such occurrences and their potential effect on the company vary from country to country and are unpredictable.

If we fail to maintain effective systems for disclosure controls and internal control over financial reporting, we may be unable to comply with the requirements of Section 404 of the Sarbanes Oxley Act of 2002 in a timely manner.

Section 404 of the Sarbanes-Oxley Act of 2002 requires us to document and test the effectiveness of its internal controls over financial reporting in accordance with an established internal control framework and to report on its conclusion as to the effectiveness of its internal controls. It also requires an independent registered public accounting firm to test our internal controls over financial reporting and report on the effectiveness of such controls for our fiscal year ending December 31, 2008 and subsequent years. It may cost us more than we expect to comply with these controls and procedure related requirements. If we discover areas of our internal controls that need improvement, we cannot be certain that any remedial measures taken will ensure that we implement and maintain adequate internal controls over financial processes and reporting in the future. Any failure to implement required new or improved controls, or difficulties encountered in their implementation could harm our operating results or cause us to fail to meet our reporting obligations.

The Company may be required to record a charge to our earnings if our goodwill becomes impaired.

The Company tests for impairment of goodwill annually at the beginning of the fourth quarter in accordance with generally accepted accounting standards. When events or changes in circumstances indicate that the carrying value for such assets may not be recoverable, however, the Company reviews its goodwill for impairment on an interim basis. Factors that may be considered a change in circumstances requiring our interim testing include a decline in stock price as compared to the Company's book value per share, future cash flows and slower growth rates. As a result of the dramatic change in the economic and market conditions in the fourth quarter of 2008, including the change in the Company's stock price as compared to its book value per share and the significant disruptions in the global credit markets, the Company performed an interim impairment test for goodwill as of the fiscal year end 2008. The Company did not record any impairment charge as a result of that interim test. However, in connection with future annual or interim tests, the Company may be required to record a non-cash charge to earnings in its financial statements during the period in which any impairment of goodwill is determined, resulting in an impact on the Company's results of operations.

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See Note 2. "Summary of Significant Accounting Policies Goodwill and Intangible Assets" in the Notes to the Consolidated Financial Statements for additional information related to impairment of goodwill.

Our business depends on effective information management systems.

We rely on our enterprise resource planning (ERP) systems to support such critical business operations as processing sales orders and invoicing, inventory control, purchasing and supply chain management, payroll and human resources, and financial reporting. We periodically implement upgrades to such systems or migrate one or more of our affiliates, facilities or operations from one system to another. If we are unable to adequately maintain such systems to support our developing business requirements or effectively manage any upgrade or migration, we could encounter difficulties that could have a material adverse impact on our business, internal controls over financial reporting, financial results, or our ability to timely and accurately report such results.

Risks Associated with KapStone's Common Stock and Warrants

The market price for our common stock may be highly volatile.

The market price of our common stock may be volatile due to certain factors, including, but not limited to; quarterly fluctuations in our financial and operating results; general conditions in the paper and packaging industries; or changes in earnings estimates.

Shares available for future issuance, conversion and exercise could have an adverse effect on the earnings per share and the market price of our common stock.

Any future issuance of equity securities, including upon exercise of outstanding warrants and stock options, could dilute the interests of our existing stockholders and could substantially decrease the trading price of our common stock. As of February 28, 2009, we have outstanding warrants to purchase approximately 37 million shares of our common stock. In addition, in connection with our initial public offering, we issued to the representative of the underwriter an option to purchase 1,000,000 units which, if exercised, would result in the issuance of an additional 1,000,000 shares of common stock and 2,000,000 warrants.

We may choose to redeem our outstanding warrants at a time that is disadvantageous to our warrant holders.

Subject to there being a current prospectus under the Securities Act of 1933 with respect to the shares of common stock issuable upon exercise of the warrants issued as a part of the units in our initial public offering, during the entire period between any notice of redemption and the actual redemption date, we may redeem the warrants at any time after the warrants become exercisable, in whole and not in part, at a price of \$.01 per warrant, upon a minimum of 30 days prior written notice of redemption, if and only if, the last sales price of our common stock equals or exceeds \$8.50 per share for any 20 trading days within a 30 trading day period ending three business days before the notice of redemption is sent. Redemption of the warrants could force the warrant holders (i) to exercise the warrants and pay the exercise price therefore at a time when it may be disadvantageous for the holders to do so, (ii) to sell the warrants at the then current market price when they might otherwise wish to hold the warrants, or (iii) to accept the nominal redemption price which, at the time the warrants are called for redemption, is likely to be substantially less than the market value of the warrants.

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Although we currently have an effective registration statement covering the issuance of the shares underlying the warrants issued in our initial public offering at the time that the warrant holders exercise their warrants, we cannot guarantee that a registration statement will continue to be effective, in which case the warrant holders may not be able to exercise their warrants.

Holders of the warrants issued in our initial public offering will be able to receive shares upon exercise of the warrants only if (i) a current registration statement under the Securities Act of 1933 relating to the shares of common stock underlying the warrants is then effective and (ii) such shares are qualified for sale or exempt from qualification under the applicable securities laws of the states in which the various holders of warrants reside. Although we currently have a current registration statement covering the shares underlying the warrants to the extent required by federal securities laws, we cannot give assurance that we will be able to maintain the effectiveness of such registration statement. In addition, some states may not permit us to register the shares issuable upon exercise of our warrants for sale. Since we have no obligation to net cash settle the warrants in the absence of an effective registration statement, the value of the warrants will be greatly reduced if a registration statement covering the shares issuable upon the exercise of the warrants is not kept current or if the securities are not qualified, or exempt from qualification, in the states in which the holders of warrants reside. Holders of warrants who reside in jurisdictions in which the shares underlying the warrants are not qualified and in which there is no exemption will be unable to exercise their warrants and would either have to sell their warrants in the open market or allow them to expire unexercised. If and when the warrants become redeemable by us, we may exercise our redemption right even if we are unable to qualify the underlying securities for sale under all applicable state securities laws. In light of the foregoing, the warrants may expire worthless and a purchaser of units may have paid the full unit purchase price solely for the share component of the units.

Our executive officers and directors control a substantial percentage of our common stock and warrants and thus may influence certain actions requiring a stockholder vote.

At December 31, 2008, our executive officers and directors own 7.7 million shares of our common stock, or approximately 27% of our total issued and outstanding common stock and held warrants to purchase an additional 4.8 million shares of our common stock. The warrants expire August 15, 2009. Accordingly, our executive officers and directors may have considerable influence over the outcome of all matters requiring approval by our stockholders, including future acquisitions and the election of directors. In addition, our board of directors is divided into three classes, each of which will generally serve for a term of two years with only one class of directors being elected in each year. At the annual meeting, as a consequence of our "staggered" board of directors, only a minority of the board of directors will be considered for election and our officers and directors, because of their ownership position, will have considerable influence regarding the outcome.

Some of our executive officers and directors may in the future become affiliated with entities engaged in business activities similar to those intended to be conducted by us and, accordingly, may have conflicts of interest in determining to which entity a particular business opportunity should be presented.

Some of our executive officers and directors may in the future become affiliated with entities, including "blank check" companies, engaged in business activities similar to those conducted by us. Additionally, our executive officers and directors may become aware of business opportunities which may be appropriate for presentation to us as well as the other entities to which they have an affiliation. Accordingly, they may have conflicts as to questions pertaining to which entity a particular business opportunity should be presented.

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Risks associated with the paper, packaging, forest products and related industries.

The paper, packaging, forest products and related industries are highly cyclical. Fluctuations in the prices of and the demand for products could result in smaller profit margins and lower sales volumes.

Historically, economic and market shifts, fluctuations in capacity and changes in foreign currency exchange rates have created cyclical changes in prices, sales volume and margins for products in the paper, packaging, forest products and related industries. The length and magnitude of industry cycles have varied over time and by product, but generally reflect changes in macroeconomic conditions and levels of industry capacity. Most paper products and many wood products used in the packaging industry are commodities that are widely available from many producers. Because commodity products have few distinguishing qualities from producer to producer, competition for these products is based primarily on price, which is determined by supply relative to demand. The overall levels of demand for these commodity products reflect fluctuations in levels of end-user demand, which depend in large part on general macroeconomic conditions in North America and regional economic conditions in our markets, as well as foreign currency exchange rates. The foregoing factors could materially and adversely impact sales and profitability of our company.

Difficulty obtaining wood fiber at favorable prices, or at all, may negatively impact companies in the packaging industry.

Wood fiber is the principal raw material in many parts of the packaging industry. Wood fiber is a commodity, and prices historically have been cyclical. Environmental litigation and regulatory developments have caused, and may cause in the future, significant reductions in the amount of timber available for commercial harvest in the United States. These reductions have caused the closure of plywood and lumber operations in some of the geographic areas in which a target company might operate. In addition, future domestic or foreign legislation and litigation concerning the use of timberlands, the protection of endangered species, the promotion of forest health and the response to and prevention of catastrophic wildfires could also affect timber supplies. Availability of harvested timber may further be limited by fire, insect infestation, disease, ice storms, wind storms, flooding and other natural and man made causes, thereby reducing supply and increasing prices.

Industry supply of commodity paper and wood products is also subject to fluctuation, as changing industry conditions can influence producers to idle or permanently close individual machines or entire mills. In addition, to avoid substantial cash costs in connection with idling or closing a mill, some producers will choose to continue to operate at a loss, sometimes even a cash loss, which could prolong weak pricing environments due to oversupply. Oversupply in these markets can also result from producers introducing new capacity in response to favorable short-term pricing trends. Industry supply of commodity papers and wood products is also influenced by overseas production capacity, which has grown in recent years and is expected to continue to grow. Wood fiber pricing is subject to regional market influences, and the cost of wood fiber may increase in particular regions due to market shifts in those regions. In addition, the ability to obtain wood fiber from foreign countries may be impacted by legal and political conditions in those countries as well as transportation difficulties.

An increase in the cost of purchased energy and raw materials would lead to higher manufacturing costs, thereby reducing margins.

Energy is a significant raw material in the paper, packaging, forest products and related industries. Energy prices, particularly for electricity, coal and fuel oil, have been volatile in recent years and currently coal and electricity exceed historical averages. These fluctuations have historically impacted manufacturing costs of companies in these industries, often contributing to earnings volatility. Recent significant increases in energy prices can be expected to adversely impact businesses in these industries.

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In addition, we could be materially adversely impacted by supply disruptions or the inability to pass on cost increases to our customers.

Paper, packaging and forest products companies face strong competition.

The paper, packaging, forest products and related industries are highly fragmented, and we face competition from numerous competitors, domestic as well as foreign. Some of our competitors will be large, vertically integrated companies that have greater financial and other resources, greater manufacturing economies of scale, greater energy self-sufficiency and/or lower operating costs.

Certain paper and wood products are vulnerable to long-term declines in demand due to competing technologies or materials.

Companies in the paper, packaging, forest products and related industries are subject to possible declines in demand for their products as the use of alternative materials and technologies grows and the prices of such alternatives become more competitive. Any substantial shift in demand from wood and paper products to competing technologies or materials could result in a material decrease in sales of our products. While we would seek to adapt our product offerings to changes in market demand, we cannot assure you that any efforts will be successful or sufficient.

Packaging companies are subject to significant environmental regulation and environmental compliance expenditures, as well as other potential environmental liabilities.

Companies in the packaging industry are subject to a wide range of general and industry-specific environmental laws and regulations, particularly with respect to air emissions, wastewater discharges, solid and hazardous waste management, site remediation, forestry operations and endangered species habitats. We may incur substantial expenditures to maintain compliance with applicable environmental laws and regulations. Failure to comply with applicable environmental laws and regulations could expose us to civil or criminal fines or penalties or enforcement actions, including orders limiting operations or requiring corrective measures, installation of pollution control equipment or other remedial actions.

Risks Associated with Acquisitions

Future acquisitions of businesses by us would subject us to additional business, operating and industry risks, the impact of which cannot presently be evaluated, and could adversely impact our capital structure.

We intend to pursue other acquisition opportunities in an effort to diversify our investments and/or grow our business. Any business acquired by us may cause us to be affected by numerous risks inherent in the acquired business' operations. If we acquire a business in an industry characterized by a high level of risk, we may be affected by the currently unascertainable risks of that industry. Although our management will endeavor to evaluate the risks inherent in a particular industry or target business, we cannot assure you that we will be able to properly ascertain or assess all of the significant risk factors.

In addition, the financing of any acquisition completed by us could adversely impact our capital structure as any such financing would likely include the issuance of additional equity securities and/or the borrowing of additional funds. The issuance of additional equity securities may significantly reduce the equity interest of our stockholders and/or adversely affect prevailing market prices for our common stock. Increasing our indebtedness could increase the risk of a default that would entitle the holder to declare all of such indebtedness due and payable and/or to seize any collateral securing the indebtedness. In addition, default under one debt instrument could in turn permit lenders under other debt instruments to declare borrowings outstanding under those other instruments to be due and payable pursuant to cross default clauses. Accordingly, the financing of future acquisitions could adversely impact our capital structure and your equity interest in us.

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Except as required by law or the rules of any securities exchange on which our securities might be listed at the time it seeks to consummate a subsequent acquisition, stockholders will not be asked to vote on any such proposed acquisition and no redemption rights in connection with any such acquisition will exist.

If the benefits of our KPB and CKD acquisitions do not meet the expectations of the marketplace, or financial or industry analysts, the market price of our common stock may decline.

We acquired KPB on January 2, 2007 and CKD on July 1, 2008. The market price of our common stock may decline if these acquisitions do not perform as expected, or we do not otherwise achieve the perceived benefits of the acquisitions as rapidly as, or to the extent anticipated by, the marketplace, or financial or industry analysts. Accordingly, investors may experience a loss as a result of a decreasing stock price and we may not be able to raise future capital, if necessary, in the equity markets.

Our operations are dependent upon certain operating agreements with IP and MWV.

We are dependent upon MWV to provide us transitional support services for a period of up to 18 months from July 1, 2008. In addition, we rely on MWV and IP for certain supply arrangements to provide us roundwood and woodchips.

Although IP has agreed to indemnify us with respect to environmental liabilities that were assumed, we may incur significant remediation and other costs if such losses exceed the cap on indemnification or occur after the expiration of the indemnification period.

The Roanoke Rapids facility operated as an industrial facility for many years prior to the enactment of environmental legislation that would have required certain pollution prevention concepts to be addressed at the facility. Due to its long history of industrial operations, the possibility of onsite and offsite environmental impact to the soil and groundwater may present a heightened risk of liability for contamination. The overall indemnification by IP for certain losses includes assumed environmental liabilities, subject to a \$1.0 million threshold and a cap of \$15.0 million. IP's indemnification for assumed environmental liabilities will survive for three years. However, with respect to environmental claims, the cap described above will be reduced by \$1.8 million every six months during the three year survival period. Because we are unable to presently make a determination as to whether the environmental impact, if any, would be widespread or significant, the negotiated cap and survival period may not be sufficient to cover future losses. Further, if we are required to make significant expenditures for remediation and other costs that exceed the cap, the cost of such efforts may have a significant negative impact on our results of operations and financial condition.

Although MWV has agreed to indemnify us with respect to environmental liabilities pertaining to the North Charleston facility, we may incur significant remediation and other costs if such losses are below the basket or exceed the cap on indemnification or occur after the expiration of the indemnification period.

Due to its past history of industrial operations at the North Charleston mill, the possibility of onsite and offsite environmental impact on soil and groundwater may present a heightened risk of liability for contamination. We did not assume responsibility for certain offsite environmental liabilities resulting from conditions existing prior to the closing. The overall indemnification by MWV for certain losses includes assumed environmental liabilities, subject to an \$8.5 million threshold and a cap equal to 15% of the purchase price of \$485 million. MWV's obligation to indemnify us for any historical onsite liability or breach of certain environmental representations and warranties terminates on December 31, 2013. MWV's indemnification for certain offsite historical liabilities survive indefinitely. Because we are unable to presently make a determination as to whether the environmental impact, if any, would be widespread or significant, the negotiated cap and survival period may not be sufficient to cover future losses. Further if we are required to make significant expenditures for remediation and

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other costs that exceed the cap, the costs of such efforts may have a significant negative impact on our results of operations and financial conditions.

The anticipated benefits of the CKD acquisition may not be realized.

We consummated the acquisition of CKD with the expectation that it would result in various benefits including, among other things, benefits relating to enhanced revenues, a broader array of product offerings, the expansion of our production capabilities, operational improvements and a diversification of our customer base. The acquisition presents challenges to management, including the integration of operations, properties and personnel of CKD and our existing operations. Achieving the anticipated benefits of the transaction is subject to a number of uncertainties, including, but not limited to, whether we can integrate our business and the CKD business in an efficient and effective manner. Failure to achieve these anticipated benefits could result in increased costs, decreases in the amount of expected revenues and diversion of management's time that could materially impact our business, financial condition and operating results.

We may fail to realize the anticipated synergies and cost savings expected from the CKD acquisition.

Our success after the CKD acquisition will depend, in part, on our ability to realize the anticipated growth opportunities and cost savings from integrating our business with CKD. To realize these anticipated benefits, we must successfully integrate our business with CKD in a manner that permits these synergies to be realized. If we are not able to successfully achieve these objectives, such anticipated benefits may not be realized fully, or at all, or may take longer to realize than expected.

We may have difficulty integrating our business with the CKD business and may incur substantial costs in connection with the integration.

Achieving the anticipated benefits of the acquisition will depend on the successful integration of our products, operations, personnel, and facilities with those of CKD in a timely and efficient manner.

Although we do not anticipate material difficulties in c