PACKAGING CORP OF AMERICA
Form 10-Q
November 07, 2018

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended September 30, 2018

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 1-15399

(Exact Name of Registrant as Specified in its Charter)

Delaware	36-4277050
(State or Other Jurisdiction of	(I.R.S. Employer Identification No.)
Incorporation or Organization)	
1 North Field Court, Lake Forest, Illinois	60045
(Address of Prinicpal Executive Offices)	(Zip Code)

Registrant's telephone number, including area code

(847) 482-3000

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

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See the definitions of “large accelerated filer,” “accelerated filer,” “smaller reporting company,” and “emerging growth company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer	Accelerated filer
Non-accelerated filer	Smaller reporting company
Emerging growth company	

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

As of November 2, 2018 the Registrant had outstanding 94,497,298 shares of common stock, par value $0.01 per share.

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All reports we file with the Securities and Exchange Commission (SEC) are available free of charge via the Electronic Data Gathering Analysis and Retrieval (EDGAR) System on the SEC website at www.sec.gov. We also provide copies of our SEC filings at no charge upon request and make electronic copies of our reports available through our website at www.packagingcorp.com as soon as reasonably practicable after filing such material with the SEC.

PART I

FINANCIAL INFORMATION

Item 1. FINANCIAL STATEMENTS
Packaging Corporation of America

Consolidated Statements of Income and Comprehensive Income

(unaudited, dollars in millions, except per-share data)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
Statements of Income:				
Net sales	$1,809.9	$1,640.1	$5,268.1	$4,760.6
Cost of sales	(1,366.7)	(1,243.1)	(4,048.2)	(3,661.2)
Gross profit	443.2	397.0	1,219.9	1,099.4
Selling, general and administrative expenses	(134.2)	(129.6)	(406.7)	(386.9)
Other expense, net	(10.5)	(24.8)	(32.2)	(32.4)
Income from operations	298.5	242.6	781.0	680.1
Interest expense, net and other	(24.4)	(25.7)	(75.0)	(75.5)
Income before taxes	274.1	216.9	706.0	604.6
Provision for income taxes	(67.4)	(77.8)	(172.6)	(204.9)
Net income	$206.7	$139.1	$533.4	$399.7
Net income per common share:				
Basic	$2.19	$1.47	$5.65	$4.24
Diluted	$2.18	$1.47	$5.64	$4.23
Dividends declared per common share	$0.79	$0.63	$2.21	$1.89
Statements of Comprehensive Income:				
Net income	$206.7	$139.1	$533.4	$399.7
Other comprehensive income, net of tax:				
Foreign currency translation adjustment	—	0.1	(0.1)	(0.2)
Reclassification adjustments to cash flow hedges included in net income, net of tax of $0.3 million, $0.5 million, $1.0 million, and $1.6 million	1.0	0.9	3.0	2.6
Amortization of pension and postretirement plans actuarial loss and prior service cost, net of tax of $1.0 million, $1.2 million, $3.0 million, and $3.7 million	3.0	1.9	8.9	6.2
Other comprehensive income	4.0	2.9	11.8	8.6
Comprehensive income	$210.7	$142.0	$545.2	$408.3

See accompanying condensed notes to unaudited quarterly consolidated financial statements.

Packaging Corporation of America

Consolidated Balance Sheets

(unaudited, dollars and shares in millions, except per-share data)

	September 30, 2018	December 31, 2017
ASSETS		
Current assets:		
Cash and cash equivalents	$ 293.8	$ 216.9
Accounts receivable, net of allowance for doubtful accounts and customer deductions of $14.0 million and $12.6 million as of September 30, 2018, and December 31, 2017, respectively	986.2	830.7
Inventories	780.6	762.5
Prepaid expenses and other current assets	49.0	35.5
Federal and state income taxes receivable	5.1	69.5
Total current assets	2,114.7	1,915.1
Property, plant, and equipment, net	3,065.1	2,924.9
Goodwill	888.7	883.2
Other intangible assets, net	373.9	410.0
Other long-term assets	57.6	64.3
Total assets	$ 6,500.0	$ 6,197.5
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Current maturities of long-term debt	$ —	$ 150.0
Capital lease obligations	1.4	1.3
Accounts payable	438.9	402.9
Dividends payable	75.8	60.5
Accrued liabilities	223.4	203.2
Accrued interest	27.0	14.8
Total current liabilities	766.5	832.7
Long-term liabilities:		
Long-term debt	2,482.9	2,480.4
Capital lease obligations	17.9	19.0
Deferred income taxes	279.3	239.5
Compensation and benefits	360.2	372.5
Other long-term liabilities	63.0	70.8
Total long-term liabilities	3,203.3	3,182.2
Commitments and contingent liabilities		
Stockholders' equity:		
Common stock, par value $0.01 per share, 300.0 million shares authorized, 94.5 million and 94.3 million shares issued as of September 30, 2018, and December 31, 2017, respectively	0.9	0.9

Additional paid in capital	488.9	471.2
Retained earnings	2,185.5	1,867.4
Accumulated other comprehensive loss	(145.1)	(156.9)
Total stockholders' equity	2,530.2	2,182.6
Total liabilities and stockholders' equity	$ 6,500.0	$ 6,197.5

See accompanying condensed notes to unaudited quarterly consolidated financial statements.

Packaging Corporation of America

Consolidated Statements of Cash Flows

(unaudited, dollars in millions)

	Nine Months Ended September 30, 2018	2017
Cash Flows from Operating Activities:		
Net income	$533.4	$399.7
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation, depletion, and amortization of intangibles	313.6	283.7
Amortization of deferred financing costs	6.5	6.0
Share-based compensation expense	17.4	15.4
Deferred income tax provision	34.9	1.6
Net loss on impairment of assets	—	13.5
Pension and post-retirement benefits expense, net of contributions	(2.7)	(25.3)
Other, net	8.2	12.0
Changes in operating assets and liabilities:		
Increase in assets —		
Accounts receivable	(148.9)	(142.2)
Inventories	(22.6)	(13.0)
Prepaid expenses and other current assets	(13.2)	(10.3)
Increase (decrease) in liabilities —		
Accounts payable	19.6	37.7
Accrued liabilities	23.7	9.6
Federal and state income taxes payable / receivable	64.6	(5.1)
Net cash provided by operating activities	834.5	583.3
Cash Flows from Investing Activities:		
Additions to property, plant, and equipment	(404.3)	(226.2)
Additions to other long term assets	(4.1)	(6.9)
Proceeds from disposals	0.5	4.4
Other, net	2.6	1.1
Net cash used for investing activities	(405.3)	(227.6)
Cash Flows from Financing Activities:		
Repayments of debt and capital lease obligations	(151.0)	(35.6)
Common stock dividends paid	(193.4)	(178.2)
Shares withheld to cover employee restricted stock taxes	(7.9)	(10.7)
Net cash used for financing activities	(352.3)	(224.5)
Net increase in cash and cash equivalents	76.9	131.2
Cash and cash equivalents, beginning of period	216.9	239.3
Cash and cash equivalents, end of period	$293.8	$370.5

See accompanying condensed notes to unaudited quarterly consolidated financial statements.

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Condensed Notes to Unaudited Quarterly Consolidated Financial Statements

1. Nature of Operations and Basis of Presentation

Packaging Corporation of America ("we," "us," "our," PCA," or the "Company") was incorporated on January 25, 1999. In April 1999, PCA acquired the containerboard and corrugated packaging products business of Pactiv Corporation (Pactiv), formerly known as Tenneco Packaging, Inc., a wholly owned subsidiary of Tenneco Inc. We are a large diverse manufacturer of both packaging and paper products. We are headquartered in Lake Forest, Illinois and we operate primarily in the United States.

We report our business in three reportable segments: Packaging, Paper, and Corporate and Other. Our Packaging segment produces a wide variety of corrugated packaging products. The Paper segment manufactures and sells a range of communication-based papers. During the second quarter of 2018, the Company discontinued the production of uncoated free sheet and coated one-side grades at the Wallula, Washington mill and converted the No. 3 machine to a virgin kraft linerboard machine. Subsequent to the date of conversion in May 2018, operating results for the Wallula mill are primarily included in the Packaging segment. Corporate and other includes support staff services and related assets and liabilities, transportation assets, and activity related to other ancillary support operations. For more information about our segments, see Note 18 Segment Information.

In these consolidated financial statements, certain amounts in prior periods' consolidated financial statements have been reclassified to conform with the current period presentation.

The consolidated financial statements of PCA as of September 30, 2018 and for the three and nine months ended September 30, 2018 and 2017 are unaudited but include all adjustments (consisting only of normal recurring adjustments) that management considers necessary for a fair presentation of such financial statements. The preparation of the consolidated financial statements involves the use of estimates and accruals. Actual results may vary from those estimates. These financial statements have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with Article 10 of Regulation S-X of the Securities and Exchange Commission (SEC). Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete audited financial statements. Operating results for the three and nine months ended September 30, 2018 are not necessarily indicative of the results that may be expected for the year ending December 31, 2018. These consolidated financial statements should be read in conjunction with our Annual Report on Form 10-K for the year ended December 31, 2017.

The consolidated financial statements include the accounts of PCA and its majority-owned subsidiaries after elimination of intercompany balances and transactions.

2. New and Recently Adopted Accounting Standards

Recently Adopted Accounting Standards

Effective January 1, 2018, the Company adopted Accounting Standards Update (“ASU”) 2014-09 (Topic 606): Revenue from Contracts with Customers. This ASU supersedes the revenue recognition requirements in Topic 605 Revenue Recognition (Topic 605) and requires entities to recognize revenue when control of the promised goods or services is transferred to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The ASU requires additional disclosure about the nature, amount, timing, and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and estimates, and changes in those estimates. The Company adopted the standard utilizing the modified retrospective method, in which case the cumulative effect was recognized at the date of initial application on January 1, 2018. The adoption of the standard did not have a material effect on the Company’s financial position or results of operations; however, the following adjustment and reclassification of certain costs were made for the three and nine months ended September 30, 2018:

a. The Company ships a portion of its products to customers under consignment agreements. These products do not have an alternative use, and, under the new standard, revenue associated with these products is required to be recognized earlier than under prior revenue recognition standards. Utilizing the modified retrospective method, the cumulative impact of adopting the new standard resulted in an increase of approximately $1.6 million, net of tax, to opening retained earnings as of January 1, 2018.

b. The new revenue standard also provides additional clarity concerning contract fulfillment costs, which resulted in certain costs being classified as cost of sales rather than selling, general and administrative expenses beginning January 1, 2018. For the three and nine months ended September 30, 2018, this amount totaled $6.9 million and $20.0 million, respectively.

See Note 3, Revenue, for more information.

Effective January 1, 2018, the Company adopted ASU 2017-07, Compensation: Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost. The guidance in this update requires that an employer disaggregate the service cost component from the other components of net benefit cost. Non-service cost components of net periodic benefit cost are required to be presented in the income statement separately from the service cost component and outside the subtotal of operating income. The update also allows only the service cost component to be eligible for capitalization for internally developed capital projects. The amendments in this update are applied retrospectively for the income statement presentations and prospectively for the capitalization of service costs.

The adoption of this ASU retrospectively resulted in a $0.3 million and $0.9 million reclassification between cost of sales and selling, general and administrative expenses (both components of income from operations) and interest expense, net and other (a component outside of income from operations) for the three and nine months ended September 30, 2017, respectively.

Effective January 1, 2018, the Company adopted ASU 2017-09, Compensation - Stock Compensation (Topic 718): Scope of Modification Accounting, which clarifies what changes to the terms or conditions of a share-based payment award require an entity to apply modification accounting in Topic 718. This ASU will be applied prospectively when changes to the terms or conditions of a share-based payment award occur.

Effective January 1, 2018, the Company adopted ASU 2017-01 (Topic 805): Clarifying the Definition of a Business, which amends the guidance in ASC 805, "Business Combinations". The ASU changes the definition of a business to assist entities with evaluating when a set of transferred assets and activities is a business. Under the new guidance, an entity first determines whether substantially all of the fair value of the gross assets acquired is concentrated in a single identifiable asset or a group of similar identifiable assets. If this threshold is met, the set is not a business. If it is not met, the entity then evaluates whether the set meets the requirements that a business include, at a minimum, an input and a substantive process that together significantly contribute to the ability to create outputs. The ASU defines an output as "the result of inputs and processes applied to those inputs that provide goods or services to customers, investment income (such as dividends or interest), or other revenues." The ASU will be applied prospectively to any transactions subsequent to adoption.

Effective January 1, 2018, the Company adopted ASU 2016-15 (Topic 230), Statement of Cash Flows: Classification of Certain Cash Receipts and Cash Payments. This ASU adds or clarifies guidance on the classification of certain cash receipts and payments in the statement of cash flows. The adoption of this guidance did not have a material impact on the Company's financial condition, results of operations, or cash flows.

New Accounting Standards Not Yet Adopted

In August 2018, the Financial Accounting Standards Board ("FASB") issued ASU 2018-14, Compensation – Retirement Benefits – Defined Benefit Plans – General (Subtopic 715-20): Disclosure Framework – Changes to the Disclosure Requirements for Defined Benefit Plans. ASU 2018-14 removes certain disclosures that are not considered cost beneficial, clarifies certain required disclosures and adds additional disclosures. The ASU is effective for annual periods beginning after December 31, 2020, with early adoption permitted. The amendments in ASU 2018-14 would need to be applied on a retrospective basis. The Company is currently evaluating the impact this guidance will have on its related disclosures.

In August 2018, the FASB issued ASU 2018-13, Fair Value Measurement (Topic 820): Disclosure Framework – Changes to the Disclosure Requirements for Fair Value Measurement. ASU 2018-13 removes or modifies certain disclosure requirements and adds additional requirements to improve the usefulness of the fair value measurement disclosure for financial statement users. The ASU is effective for annual and interim periods beginning after December 15, 2019, with early adoption permitted. Certain amendments of ASU 2018-13 are required to be applied prospectively for the first interim period of the initial year of adoption. All other amendments need to be applied retrospectively. The Company is currently evaluating the impact of the new guidance.

In February 2018, the FASB issued ASU 2018-02 (Topic 220): Income Statement – Reporting Comprehensive Income – Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income, which allows for optional reclassification from accumulated other comprehensive income to retained earnings for the stranded tax effects resulting from the enactment of H.R.1 (P.L. 115-97), originally known as the "Tax Cuts and Jobs Act," in December 2017. An entity that elects to reclassify these amounts must reclassify stranded tax effects related to the change in federal tax rate for all items accounted for in other comprehensive income (e.g., pension and postretirement benefits and cash flow hedges). Entities may also elect to reclassify other stranded tax effects that relate to the Act but do not directly relate to the change in the federal tax rate (e.g., state taxes). Upon adoption of ASU 2018-02, entities are required to disclose their policy for releasing the income tax effects from accumulated other comprehensive income. ASU 2018-02 is effective for annual periods beginning after December 15, 2018, and interim periods within those fiscal years. Early adoption is permitted. The Company does not expect this ASU to have a material impact on the Company’s financial position, results of operations, or cash flow.

In February 2016, the FASB issued ASU 2016-02 (Topic 842): Leases. This ASU amends a number of aspects of lease accounting, including requiring lessees to recognize operating leases with a term greater than one year on their balance sheet as a right-of-use asset and corresponding lease liability, measured at the present value of the lease payments. Additionally, the guidance requires qualitative and quantitative disclosures designed to assess the amount, timing and uncertainty of cash flows arising from leases. In July 2018, the FASB issued ASU 2018-10: Codification Improvements to Topic 842, Leases and ASU 2018-11: Leases (Topic 842): Targeted Improvements. These ASUs provide clarification to the lease standard and allow entities an optional transition method for implementing ASU 2016-02 and a lessor practical expedient for separating lease and non-lease components. The optional transition method allows companies the option to use the effective date as the date of initial application on transition. The Company plans to elect this transition method, and as a result, we will not adjust our comparative period financial information or make the new required lease disclosures for periods before the effective date.

ASU 2016-02 is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years, and early adoption is permitted. We are in the process of implementing changes to our systems and processes in conjunction with our review of existing lease agreements, which primarily consist of equipment and real estate leases. In addition, we are currently working with a vendor to implement a technology tool to assist with the accounting and reporting requirements of the new standard. We will adopt Topic 842 effective January 1, 2019 and expect to elect certain available transitional practical expedients. We are still in the process of determining the effects on our financial statements but do expect to recognize a liability and corresponding asset associated with in-scope operating leases.

There were no other accounting standards recently issued that had or are expected to have a material impact on our financial position or results of operations.

3. Revenue

Revenue Recognition

Revenue is recognized when control of the promised goods or services is transferred to customers in an amount that reflects the consideration expected to be entitled in exchange for those goods or services. Sales, value added, and other taxes collected concurrently with revenue-producing activities are excluded from revenue.

The following table presents our revenues disaggregated by product line (dollars in millions):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017 (a)	2018	2017 (a)
Packaging	$1,535.1	$1,346.6	$4,434.2	$3,915.0
Paper	254.3	271.4	774.5	784.3
Corporate and other	20.5	22.1	59.4	61.3
Total revenue	$1,809.9	$1,640.1	$5,268.1	$4,760.6

(a) Prior periods have not been adjusted under the modified retrospective method for Topic 606.

Packaging Revenue

Our containerboard mills produce linerboard and semi-chemical corrugating medium which are papers primarily used in the production of corrugated products. The majority of our containerboard production is used internally by our corrugated products manufacturing facilities. The remaining containerboard is sold to outside domestic and export customers. Our corrugated products manufacturing plants produce a wide variety of corrugated packaging products and retail merchandise displays. We sell corrugated products to national, regional and local accounts, which are broadly diversified across industries and geographic locations.

The Company recognizes revenue for its packaging products when performance obligations under the terms of a contract with a customer are satisfied. This occurs with the transfer of control of our products at a specific point in time. Based on our express terms and conditions of the sale of products to our customers, as well as terms included in contractual arrangements with our customers, we do not have an enforceable right of payment that includes a reasonable profit throughout the duration of the contract for products that do not have an alternative use. Revenue is recognized when the product is shipped from the mill or from our manufacturing facility to our customer. Certain customers may receive volume-based incentives, which are accounted for as variable consideration. We estimate these amounts based on the expected amount to be provided to customers and reduce revenue recognized.

Certain customers receive a portion of their packaging products as consigned inventory with billing triggered once the customer uses or consumes the designated product. Prior to invoicing, these amounts are handled as unbilled receivables. Total unbilled receivables, which are immaterial in amount, are included in the accounts receivable financial statement caption.

Paper Revenue

We manufacture and sell a range of communication-based papers. Communication papers consist of cut-size office papers, and printing and converting papers. Pressure sensitive papers, including release liners, are used for specialty applications such as consumer and commercial product labels.

The Company recognizes revenue for its paper products when performance obligations under the terms of a contract with a customer are satisfied. This occurs with the transfer of control of our products at a specific point in time. Revenue is recognized when the product is shipped from the mill or from our manufacturing facility or distribution center to our customer. Certain customers may receive volume-based incentives, which are accounted for as variable consideration. We estimate these amounts based on the expected amount to be provided to customers and reduce revenue recognized.

Corporate and Other Revenue

Revenue in this segment primarily relates to Louisiana Timber Procurement Company, L.L.C. (LTP), a variable-interest entity that is 50% owned by PCA and 50% owned by Boise Cascade Company (Boise Cascade). PCA is the primary beneficiary of LTP and has the power to direct the activities that most significantly affect the economic performance of LTP. Therefore, we consolidate 100% of LTP in our financial statements. See Note 17, Transactions With Related Parties, for more information related to LTP.

The Company recognizes revenue within this segment when performance obligations under the terms of a contract with a customer are satisfied. This occurs with the transfer of control of our products at a specific point in time.

Practical Expedients and Exemption

Shipping and handling fees billed to a customer are recorded on a gross basis in "Net sales" with the corresponding shipping and handling costs included in "Cost of sales" in the concurrent period as the revenue is recorded. We expense sales commissions when incurred because the amortization period is one year or less. Sales commissions are recorded in "Selling, general, and administrative expenses".

We do not disclose the value of unsatisfied performance obligations for contracts with an original expected duration of one year or less.

4. Acquisitions

Sacramento Container Acquisition

On October 2, 2017, PCA acquired substantially all of the assets of Sacramento Container Corporation, and 100% of the membership interests of Northern Sheets, LLC and Central California Sheets, LLC (collectively referred to as “Sacramento Container”) for a purchase price of $274 million, including working capital adjustments. Funding for the $274 million purchase price came from available cash on hand. Assets acquired include full-line corrugated products and sheet feeder operations in both McClellan, California and Kingsburg, California. Sacramento Container provides packaging solutions to customers serving portions of California’s strong agricultural market. Sacramento Container’s financial results are included in the Packaging segment from the date of acquisition.

The Company accounted for the Sacramento Container acquisition using the acquisition method of accounting in accordance with ASC 805, Business Combinations. The total purchase price has been allocated to tangible and intangible assets acquired and liabilities assumed based on respective fair values, as follows (dollars in millions):

	12/31/2017 Allocation	Adjustments	Revised Allocation
Goodwill	$ 151.1	$ 5.5	$ 156.6
Other intangible assets	72.6	(5.5)	67.1
Property, plant and equipment	26.7	—	26.7
Other net assets	23.4	—	23.4
Net assets acquired	$ 273.8	$ —	$ 273.8

During the second quarter ended June 30, 2018, we made a $5.5 million net adjustment based on the final valuation of the intangible assets. We recorded the adjustment as a decrease to other intangible assets with an offset to goodwill.

Goodwill is calculated as the excess of the purchase price over the fair value of the net assets acquired. Among the factors that contributed to the recognition of goodwill were Sacramento Container’s commitment to continuous improvement and regional synergies, as well as the expected increases in PCA’s containerboard integration levels. Goodwill is deductible for tax purposes.

Other intangible assets, primarily customer relationships, were assigned an estimated weighted average useful life of 9.6 years.

Property, plant, and equipment were assigned estimated useful lives ranging from one to 13 years.

5. Earnings Per Share

The following table sets forth the computation of basic and diluted income per common share for the periods presented (dollars and shares in millions, except per share data):

	Three Months Ended September 30,		Nine Months Ended September 30,	
Numerator:	2018	2017	2018	2017
Net income	$206.7	$139.1	$533.4	$399.7
Less: distributed and undistributed earnings allocated to participating securities	(1.6)	(1.1)	(4.1)	(3.4)
Net income attributable to common shareholders	$205.1	$138.0	$529.3	$396.3
Denominator:				
Weighted average basic common shares outstanding	93.7	93.6	93.7	93.5
Effect of dilutive securities	0.3	0.2	0.2	0.2
Weighted average diluted common shares outstanding	94.0	93.8	93.9	93.7
Basic income per common share	$2.19	$1.47	$5.65	$4.24
Diluted income per common share	$2.18	$1.47	$5.64	$4.23

6. Other Income (Expense), Net

The components of other income (expense), net, were as follows (dollars in millions):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
Asset disposals and write-offs	$(5.1)	$(3.9)	$(14.4)	$(8.6)
Wallula mill restructuring (a)	(3.7)	(22.7)	(11.6)	(22.7)
Facilities closure and other costs (b)	(1.5)	(0.9)	(1.6)	(1.9)
Acquisition and integration related costs (c)	(0.1)	(0.5)	(0.1)	(0.8)
Insurance deductible for property damage (d)	(0.5)	—	(0.5)	—
DeRidder mill incident (e)	—	2.6	—	0.1
Hexacomb working capital adjustment (f)	—	—	—	2.3
Other	0.4	0.6	(4.0)	(0.8)
Total	$(10.5)	$(24.8)	$(32.2)	$(32.4)

(a) Includes charges related to the discontinuation of production of uncoated free sheet and coated one-side grades at the Wallula, Washington mill in the second quarter of 2018 and the conversion of the No. 3 paper machine to a high-performance 100% virgin kraft linerboard machine.

(b) For 2018, includes charges consisting of closure costs related to corrugated products facilities. For 2017, includes charges consisting of closure costs related to corrugated products facilities and a paper administration facility and costs related to a lump sum settlement payment of a multiemployer pension plan for one of our corrugated products facilities.

(c) Includes charges related to recent acquisitions and the integration of recent acquisitions.

(d) For 2018, includes charges for the property damage insurance deductible for a weather-related incident at one of our corrugated products facilities.

(e) Includes the property damage and business interruption insurance recoveries and corresponding costs related to the February 2017 explosion at our DeRidder, Louisiana mill.

(f) Includes income related to a working capital adjustment from the April 2015 sale of our Hexacomb corrugated manufacturing operations in Europe and Mexico.

7. Income Taxes

On December 22, 2017, the President signed into law H.R.1 (P.L. 115-97), originally known as the “Tax Cuts and Jobs Act” (the “Tax Act”). The Tax Act significantly revises the U.S. tax code by, among other items, reducing the federal corporate tax rate from 35% to 21%, providing for the full expensing of certain depreciable property, eliminating the corporate alternative minimum tax, limiting the deductibility of interest expense, further limiting the deductibility of certain executive compensation, limiting the use of net operating loss carryforwards created in tax years beginning after December 31, 2017, and implementing a territorial tax system imposing a deemed repatriation transition tax (“Transition Tax”) on earnings of foreign subsidiaries.

The SEC staff issued Staff Accounting Bulletin (“SAB”) 118, Income Tax Accounting Implications of the Tax Cuts and Jobs Act, which provides guidance on accounting for the effects and includes a measurement period that ends when a company has obtained, prepared, and analyzed the information necessary to finalize its accounting of the Tax Act, which cannot extend beyond one year. In accordance with SAB 118, the Company recorded provisional estimates of the income tax effects of the Tax Act in the 2017 Form 10-K.

During the three and nine months ended September 30, 2018, we have recorded an immaterial favorable adjustment for the Transition Tax originally recorded with the measurement period provisional estimates at December 31, 2017. We expect to record our final adjustment for the income tax effects of the Tax Act after the completion and filing of our 2017 federal and state income tax returns during the fourth quarter and before the SAB 118 measurement period ends. We estimate this final adjustment, primarily from favorable timing item differences, to also be immaterial.

For the three months ended September 30, 2018 and 2017, we recorded $67.4 million and $77.8 million of income tax expense and had an effective tax rate of 24.6% and 35.9%, respectively. For the nine months ended September 30, 2018 and 2017, we recorded $172.6 million and $204.9 million of income tax expense and had an effective tax rate of 24.4% and 33.9%, respectively. The decrease in our effective tax rate for both the three and nine months ended September 30, 2018 compared with the same periods in 2017 was primarily due to the Tax Act (P.L. 115-97), which included a reduction in the federal tax rate of 14.0% offset by the loss of the Domestic Production Activities Deduction benefit of about 3.2% and a reduction in the federal benefit of state tax deductions of about 0.8%, as well as an internal legal entity consolidation that took place in the third quarter of 2017, partially offset by lower excess tax benefits from employee share-based payment awards under ASU 2016-09 in 2018 compared to the same periods in 2017.

Our effective tax rate may differ from the federal statutory income tax rate of 21.0% due primarily to the effect of state and local income taxes. During the nine months ended September 30, 2018 and 2017, cash paid for taxes, net of refunds received, was $73.2 million and $208.3 million, respectively. The decrease in cash tax payments between the periods is due to the lower statutory tax rate and a federal overpayment carryforward from the 2017 tax year into the 2018 tax year as a result of Tax Act related changes.

During the three and nine months ended September 30, 2018, there were no significant changes to our uncertain tax positions. For more information, see Note 6, Income Taxes, of the Notes to Consolidated Financial Statements in "Part II, Item 8. Financial Statements and Supplementary Data" of our 2017 Annual Report on Form 10-K.

8. Inventories

We value our raw materials, work in process, and finished goods inventories using lower of cost, as determined by the average cost method, or market. Supplies and materials are valued at the first-in, first-out (FIFO) or average cost methods.

The components of inventories were as follows (dollars in millions):

	September 30, 2018	December 31, 2017
Raw materials	$ 317.9	$ 279.8
Work in process	14.9	12.6
Finished goods	180.4	217.0
Supplies and materials	267.4	253.1
Inventories	$ 780.6	$ 762.5

9. Property, Plant, and Equipment

The components of property, plant, and equipment were as follows (dollars in millions):

	September 30, 2018	December 31, 2017
Land and land improvements	$ 162.0	$ 156.0
Buildings	756.2	729.8
Machinery and equipment	5,356.7	5,162.5
Construction in progress	240.6	194.5
Other	72.8	68.4
Property, plant and equipment, at cost	6,588.3	6,311.2
Less accumulated depreciation	(3,523.2)	(3,386.3)
Property, plant, and equipment, net	$ 3,065.1	$ 2,924.9

Depreciation expense for the three months ended September 30, 2018 and 2017 was $89.0 million and $87.0 million, respectively. During the nine months ended September 30, 2018 and 2017, depreciation expense was $275.3 million and $253.0 million, respectively. We recognized $14.0 million of incremental depreciation expense during the nine months ended September 30, 2018 as a result of shortening the useful lives of certain assets related to the Wallula mill restructuring and a corporate administration facility.

At September 30, 2018 and December 31, 2017, purchases of property, plant, and equipment included in accounts payable were $46.2 million and $29.8 million, respectively.

10. Goodwill and Intangible Assets

Goodwill

Goodwill represents the excess of the cost of an acquired business over the fair value of the identifiable tangible and intangible assets acquired and liabilities assumed in a business combination. At September 30, 2018 and December 31, 2017 we had $833.5 million and $828.0 million of goodwill recorded in our Packaging segment, respectively. At both September 30, 2018 and December 31, 2017, we had $55.2 million of goodwill recorded in our Paper segment.

Changes in the carrying amount of our goodwill are as follows (dollars in millions):

	Goodwill
Balance at January 1, 2018	$ 883.2
Acquisitions (a)	5.5
Balance at September 30, 2018	$ 888.7

(a) During the nine months ended September 30, 2018, the Company recorded a $5.5 million adjustment to increase the goodwill balance for the Company's October 2017 acquisition of Sacramento Container.

Intangible Assets

Intangible assets are primarily comprised of customer relationships and trademarks and trade names.

The weighted average remaining useful life, gross carrying amount, and accumulated amortization of our intangible assets were as follows (dollars in millions):

	September 30, 2018			December 31, 2017		
	Weighted Average Remaining Useful Life (in Years)	Gross Carrying Amount	Accumulated Amortization	Weighted Average Remaining Useful Life (in Years)	Gross Carrying Amount	Accumulated Amortization
Customer relationships (a)	11.2	$ 491.4	$ 135.5	11.8	$ 497.8	$ 109.8
Trademarks and trade names (a)	10.4	33.9	17.6	9.8	32.9	13.2
Other (a)	3.1	4.3	2.6	3.6	4.3	2.0
Total intangible assets (excluding goodwill)	11.1	$ 529.6	$ 155.7	11.7	$ 535.0	$ 125.0

(a) In connection with the October 2017 acquisition of Sacramento Container, the Company recorded intangible assets of $68.4 million for customer relationships, $4.1 million for trade names, and $0.1 million for other intangibles. During the second quarter ended June 30, 2018, the Company made a $5.5 million net adjustment based on the final valuation received for the intangible assets. This adjustment resulted in a revision to the original allocations for customer relationships and trade names. As of June 30, 2018, the revised allocations for customer relationships and trade names were $61.9 million and $5.1 million, respectively.

During the three months ended September 30, 2018 and 2017, amortization expense was $10.2 million and $8.4 million, respectively. During the nine months ended September 30, 2018 and 2017, amortization expense was $30.7 million and $25.3 million, respectively.

11. Accrued Liabilities

The components of accrued liabilities were as follows (dollars in millions):

	September 30, 2018	December 31, 2017
Compensation and benefits	$ 131.1	$ 127.5
Medical insurance and workers' compensation	27.0	23.9
Customer volume discounts and rebates	21.5	23.4
Franchise, property, sales and use taxes	21.3	16.0
Environmental liabilities and asset retirement obligations	4.7	4.0
Severance, retention, and relocation	3.3	3.1
Other	14.5	5.3
Total	$ 223.4	$ 203.2

12. Debt

At September 30, 2018 and December 31, 2017, our long-term debt and interest rates on that debt were as follows (dollars in millions):

	September 30, 2018		December 31, 2017	
	Amount	Interest Rate	Amount	Interest Rate
6.50% Senior Notes due March 2018	$—	— %	$150.0	6.50 %
2.45% Senior Notes, net of discount of $0.4 million and $0.5 million as of September 30, 2018 and December 31, 2017, respectively, due December 2020	499.6	2.45 %	499.5	2.45 %
3.90% Senior Notes, net of discount of $0.1 million and $0.2 million as of September 30, 2018 and December 31, 2017, respectively, due June 2022	399.9	3.90 %	399.8	3.90 %
4.50% Senior Notes, net of discount of $1.1 million and $1.2 million as of September 30, 2018 and December 31, 2017, respectively, due November 2023	698.9	4.50 %	698.8	4.50 %
3.65% Senior Notes, net of discount of $0.7 million and $0.8 million as of September 30, 2018 and December 31, 2017, respectively, due September 2024	399.3	3.65 %	399.2	3.65 %
3.40% Senior Notes, net of discount of $1.5 million and $1.6 million as of September 30, 2018 and December 31, 2017, respectively, due December 2027	498.5	3.40 %	498.4	3.40 %
Total	2,496.2	3.64 %	2,645.7	3.80 %
Less current portion	—	— %	150.0	6.50 %
Less unamortized debt issuance costs	13.3		15.3	
Total long-term debt	$2,482.9	3.64 %	$2,480.4	3.64 %

During the nine months ended September 30, 2018, we used cash on hand to repay debt outstanding of $150.0 million under the 6.50% Senior Notes due March 2018. For the nine months ended September 30, 2018 and 2017, cash payments for interest were $58.6 million and $67.2 million, respectively.

Included in interest expense, net and other, are amortization of treasury lock settlements and amortization of financing costs. For the three months ended September 30, 2018 and 2017, amortization of treasury lock settlements was $1.3 million and $1.4 million, respectively, and for the nine months ended September 30, 2018 and 2017, amortization of treasury locks was $4.0 million and $4.2 million, respectively. For the three months ended September 30, 2018 and 2017, amortization of financing costs was $0.7 million and $0.5 million, respectively, and during the nine months ended September 30, 2018 and 2017, amortization of financing costs was $2.0 million and $1.5 million, respectively.

At September 30, 2018, we had $2,496.2 million of fixed-rate senior notes outstanding. The fair value of our fixed-rate debt was estimated to be $2,478.0 million. The difference between the book value and fair value is due to the difference between the period-end market interest rate and the stated rate of our fixed-rate debt. We estimated the fair value of our fixed-rate debt using quoted market prices (Level 2 inputs) within the fair value hierarchy, which is further defined in Note 2, Summary of Significant Accounting Policies, of the Notes to Consolidated Financial Statements in "Part II, Item 8. Financial Statements and Supplementary Data" of our 2017 Annual Report on Form 10-K.

For more information on our long-term debt and interest rates on that debt, see Note 9, Debt, of the Notes to Consolidated Financial Statements in "Part II, Item 8. Financial Statements and Supplementary Data" of our 2017 Annual Report on Form 10-K.

13. Employee Benefit Plans and Other Postretirement Benefits

The components of net periodic benefit cost for our pension plans were as follows (dollars in millions):

	Pension Plans			
	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
Service cost	$6.3	$5.8	$18.8	$18.0
Interest cost	10.6	10.4	31.8	31.1
Expected return on plan assets	(14.2)	(13.5)	(42.5)	(40.5)
Net amortization of unrecognized amounts				
Prior service cost	1.8	1.4	5.2	4.4
Actuarial loss	2.3	1.9	7.0	5.7
Net periodic benefit cost	$6.8	$6.0	$20.3	$18.7

PCA makes pension plan contributions that are sufficient to fund its actuarially determined costs, generally equal to the minimum amounts required by the Employee Retirement Income Security Act (ERISA). From time to time, PCA may make additional discretionary contributions based on the funded status of the plans, tax deductibility, income from operations, and other factors. During the three and nine months ended September 30, 2018 and 2017, payments to our nonqualified pension plans were insignificant. For the three and nine months ended September 30, 2018, we made contributions of $18.0 million and $21.2 million, respectively, to our qualified pension plans, which exceeded our 2018 minimum pension contributions of $4.6 million. We made contributions of $36.2 million and $42.1 million to our qualified plans during the three and nine months ended September 30, 2017, respectively.

The components of net periodic benefit cost for our postretirement plans were as follows (dollars in millions):

	Postretirement Plans			
	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
Service cost	$0.1	$0.1	$0.2	$0.2
Interest cost	0.1	0.2	0.4	0.5
Net amortization of unrecognized amounts				
Prior service cost	(0.1)	(0.1)	(0.2)	(0.1)
Actuarial income	—	(0.1)	(0.1)	(0.1)
Net periodic benefit cost	$0.1	$0.1	$0.3	$0.5

14. Share-Based Compensation

The Company has a long-term equity incentive plan, which allows for grants of restricted stock, performance awards, stock appreciation rights, and stock options to directors, officers, and employees, as well as others who engage in services for PCA. The plan, as amended, terminates May 1, 2023 and authorizes 10.6 million shares of common stock for grant over the life of the plan. As of September 30, 2018, 0.7 million shares were available for future grants under the plan. Forfeitures are added back to the pool of shares of common stock available to be granted at a future date.

The following table presents restricted stock and performance unit award activity for the nine months ended September 30, 2018:

	Restricted Stock		Performance Units	
	Shares	Weighted Average Grant-Date Fair Value	Shares	Weighted Average Grant-Date Fair Value
Outstanding at January 1, 2018	739,732	$77.23	226,558	$77.07
Granted	173,144	114.63	87,022	115.33
Vested	(163,436)	67.28	(46,876)	74.46
Forfeitures	(3,738)	81.04	—	—
Outstanding at September 30, 2018	745,702	$88.07	266,704	$90.01

Compensation Expense

Our share-based compensation expense is recorded in "Selling, general, and administrative expenses." Compensation expense for share-based awards recognized in the Consolidated Statements of Income, net of forfeitures, was as follows (dollars in millions):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
Restricted stock	$ 4.9	$ 3.8	$ 13.9	$ 11.3
Performance units	1.7	1.4	3.5	4.1
Total share-based compensation expense	6.6	5.2	17.4	15.4
Income tax benefit	(1.6)	(2.0)	(4.4)	(5.9)
Share-based compensation expense, net of tax benefit	$ 5.0	$ 3.2	$ 13.0	$ 9.5

The fair value of restricted stock is determined based on the closing price of the Company’s stock on the grant date. Compensation expense, net of estimated forfeitures, is recorded over the requisite service period. As PCA’s Board of Directors has the ability to accelerate the vesting of these awards upon an employee’s retirement, the Company accelerates the recognition of compensation expense for certain employees approaching normal retirement age.

Performance unit awards are earned based on the achievement of defined performance rankings of Return on Invested Capital (ROIC) or Total Shareholder Return (TSR) compared to ROIC and TSR for peer companies. For performance unit awards made in 2018, 50% used TSR as the performance measure and 50% used ROIC as the performance measure. All units awarded before 2018 used ROIC as the performance measure. The ROIC component of performance unit awards are valued based on the closing price of the stock on the grant date. As the ROIC component contains a performance condition, compensation expense, net of estimated forfeitures, is recorded over the requisite service period based on the most probable number of awards expected to vest. The TSR component of performance unit awards is valued using a Monte Carlo simulation as the TSR component contains a market condition. The Monte Carlo simulation estimates the fair value of the TSR component based on the expected term of the award, a risk-free interest rate, expected dividends, and expected volatility of the Company's common stock and the common stock of the peer companies. Compensation expense is recorded ratably over the expected term of the award.

The unrecognized compensation expense for all share-based awards at September 30, 2018 was as follows (dollars in millions):

	September 30, 2018	
	Unrecognized Compensation Expense	Remaining Weighted Average Recognition Period (in years)
Restricted stock	$ 36.5	2.5
Performance units	15.7	3.1
Total unrecognized share-based compensation expense	$ 52.2	2.7

15. Stockholders' Equity
Dividends

During the nine months ended September 30, 2018, we paid $193.4 million of dividends to shareholders. On May 15, 2018, PCA announced an increase of its quarterly cash dividend on its common stock from an annual payout of $2.52 per share to $3.16 per share. On August 30, 2018, PCA's Board of Directors declared a regular quarterly cash dividend of $0.79 per share of common stock, which was paid on October 15, 2018 to shareholders of record as of September 14, 2018. The dividend payment was $74.7 million.

Repurchases of Common Stock

On February 25, 2016, PCA announced that its Board of Directors authorized the repurchase of $200.0 million of the Company's outstanding common stock. Repurchases may be made from time to time in open market or privately negotiated transactions in accordance with applicable securities regulations. The timing and amount of repurchases will be determined by the Company in its discretion based on factors such as PCA's stock price and market and business conditions.

The Company did not repurchase any shares of its common stock under this authority during the three and nine months ended September 30, 2018. At September 30, 2018, $193.0 million of the authorized amount remained available for repurchase of the Company's common stock.

Accumulated Other Comprehensive Income (Loss)

Changes in accumulated other comprehensive income (loss) (AOCI) by component were as follows (dollars in millions). Amounts in parentheses indicate losses:

	Foreign Currency Translation Adjustments	Unrealized Loss On Treasury Locks, Net	Unrealized Loss on Foreign Exchange Contracts	Unfunded Employee Benefit Obligations	Total
Balance at January 1, 2018	$ (0.3)	$ (14.2)	$ (0.3)	$ (142.1)	$(156.9)
Amounts reclassified from AOCI, net of tax	(0.1)	3.0	—	8.9	11.8
Balance at September 30, 2018	$ (0.4)	$ (11.2)	$ (0.3)	$ (133.2)	$(145.1)

Reclassifications out of AOCI were as follows (dollars in millions). Amounts in parentheses indicate expenses in the Consolidated Statements of Income:

Details about AOCI Components	Amounts Reclassified from AOCI Three Months Ended September 30, 2018	2017	Nine Months Ended September 30, 2018	2017	
Unrealized loss on treasury locks, net (a)	$(1.3)	$(1.4)	$(4.0)	$(4.2)	See (a) below
	0.3	0.5	1.0	1.6	Tax benefit
	$(1.0)	$			