GEORGIA PACIFIC CORP
Form 10-Q
August 13, 2002

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D. C. 20549

FORM 10-Q

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

For the quarterly period ended June 29, 2002

or

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

For the transition period from ______ to ______

Commission File Number 1 - 3506

GEORGIA-PACIFIC CORPORATION
(Exact Name of Registrant as Specified in its Charter)

GEORGIA	93-0432081
(State of Incorporation)	(IRS Employer Id. Number)

133 PEACHTREE STREET, N.E., ATLANTA, GEORGIA 30303
(Address of Principal Executive Offices)

(404) 652 - 4000
(Telephone Number of Registrant)

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 and Exchange Act of 1934 during the preceding 12 months and (2) has been subject to such filing requirements for the past 90 days. Yes __X__ No ____

As of the close of business on August 6, 2002, Georgia-Pacific Corporation had 232,044,236 shares of Georgia-Pacific Common Stock outstanding.

PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

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

	Second Quarter		First Six Months	
(In millions, except per share amounts)	2002	2001	2002	2001
Net sales	$ 6,222	$ 6,603	$ 12,018	$ 12,920
Costs and expenses:				
Cost of sales, excluding depreciation and amortization	4,831	5,067	9,282	10,054
Selling and distribution	500	514	994	1,026
Depreciation and amortization	260	351	519	706
General and administrative	267	268	532	549
Interest	221	289	454	599
Asset impairments	208	58	208	115
Other loss (income), net	7	(23)	10	(27)
Total costs and expenses	6,294	6,524	11,999	13,022
(Loss) income from continuing operations before income	(72)	79	19	(102)
taxes	11	50	41	5
Provision for income taxes				
(Loss) income from continuing operations	(83)	29	(22)	(107)
Income from discontinued operation, net of taxes	-	36	-	58
(Loss) income before extraordinary loss and accounting	(83)	65	(22)	(49)
change	-	-	-	(12)
Extraordinary loss from early retirement of debt, net of	-	-	(545)	11
taxes				
Cumulative effect of accounting change, net of taxes				
Net (loss) income	$ (83)	$ 65	$ (567)	$ (50)
Continuing Operations:				
	$ (83)	$ 29	$ (22)	$ (107)
	-	-	-	(12)
(Loss) income from continuing operations	-	-	(545)	11
Extraordinary loss, net of taxes				

Cumulative effect of accounting change, net of taxes				
Net (loss) income	$ (83)	$ 29	$ (567)	$ (108)
Basic and diluted per share:				
	$ (0.36)	$ 0.13	$ (0.10)	$ (0.47)
	-	-	-	(0.05)
(Loss) income from continuing operations	-	-	(2.37)	0.04
Extraordinary loss, net of taxes				
Cumulative effect of accounting change, net of taxes				
Net (loss) income	$ (0.36)	$ 0.13	$ (2.47)	$ (0.48)

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

	Second Quarter		First Six Months	
(In millions, except per share amounts)	2002	2001	2002	2001
Shares (denominator):				
Weighted average shares outstanding	230.0	226.4	229.9	225.9
Dilutive securities:				
Options	-	2.3	-	-
Employee stock purchase plans	-	0.3	-	-
Total assuming conversion	230.0	229.0	229.9	225.9
Discontinued Operation:				
	$ -	$ 36	$ -	$ 58
	$ -	$ 0.45	$ -	$ 0.72
Net income	$ -	$ 0.44	$ -	$ 0.71
Basic net income per common share				
Diluted net income per common share				
Shares (denominator):				
Weighted average shares outstanding	-	80.7	-	80.6
Dilutive securities:				
Options	-	0.8	-	0.7
Total assuming conversion	-	81.5	-	81.3

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

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

	First Six Months	
(In millions)	2002	2001
Cash flows from operating activities		
	$ (567)	$ (50)
Net loss	545	(11)
Adjustments to reconcile net income to cash provided by operations:	208	115
Cumulative effect of accounting change, net of taxes	10	(27)
Asset impairment	519	719
Other loss (income)	(62)	9
Depreciation and amortization	(237)	(57)
Deferred income taxes	-	12
Change in working capital	3	(39)
Tax benefit on stock options		
Other		
Cash provided by operations	419	671
Cash flows from investing activities		
	(268)	(382)
	-	(22)
Property, plant and equipment investments	-	(68)
Timber and timberland purchases	22	694
Acquisitions	(4)	(2)
Net proceeds from sales of assets		
Other		
Cash (used for) provided by investing activities	(250)	220
Cash flows from financing activities		
	(1,889)	(1,174)
	1,797	1,339
Repayments of long-term debt	(76)	(857)

Additions to long-term debt	70	(134)
Net decrease in short-term debt	(58)	(97)
Net increase (decrease) in bank overdrafts	3	72
Cash dividends paid	(3)	(30)
Proceeds from option plan exercises		
Fees paid to issue debt		
Cash used for financing activities	(156)	(881)
Increase in cash	13	10
Balance at beginning of period	31	40
Balance at end of period	$ 44	$ 50

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

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

(In millions, except shares and per share amounts)	June 29, 2002	December 29, 2001
ASSETS		
Current assets		
Cash	$ 44	$ 31
Receivables, less allowances of $45 and $39, respectively	2,588	2,352
Inventories	2,506	2,512
Deferred income tax assets	98	101
Other current assets	492	464
Total current assets	5,728	5,460
Property, plant and equipment		
Land, buildings, machinery and equipment, at cost	19,002	18,843
Accumulated depreciation	(9,477)	(9,051)
Property, plant and equipment, net	9,525	9,792
Goodwill, net	7,609	8,265
Intangible assets, net	702	713

Other assets	2,031	2,134
Total assets	$ 25,595	$ 26,364

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

(In millions, except shares and per share amounts)	June 29, 2002	December 29, 2001
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities		
Commercial paper and other short-term notes	$ 2,208	$ 2,284
Current portion of long-term debt	189	572
Accounts payable	1,716	1,630
Accrued compensation	269	300
Other current liabilities	920	1,024
Total current liabilities	5,302	5,810
Long-term debt, excluding current portion	9,689	9,358
Senior deferrable notes	863	863
Other long-term liabilities	3,621	3,582
Deferred income tax liabilities	1,763	1,846
Commitments and contingencies (Note 13)		
Shareholders' equity		
Common stock	184	184
par value $.80; 400,000,000 shares authorized; 230,277,000 and 230,095,000 shares issued	2,528	2,521
Additional paid-in capital	1,696	2,321
Retained earnings	(3)	(3)

Long-term incentive plan deferred compensation	(48)	(118)
Accumulated other comprehensive loss		
Total shareholders' equity	4,357	4,905
Total liabilities and shareholders' equity	$ 25,595	$ 26,364

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

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

	Second Quarter		First Six Months	
(In millions)	2002	2001	2002	2001
Net (loss) income	$ (83)	$ 65	$ (567)	$ (50)
Other comprehensive income (loss), net of tax:				
Foreign currency translation adjustments	129	(9)	120	(35)
Derivative instruments	10	(4)	21	(22)
Minimum pension liability adjustment	1	-	(71)	1
Comprehensive income (loss)	$ 57	$ 52	$ (497)	$ (106)

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

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)
GEORGIA-PACIFIC CORPORATION
JUNE 29, 2002

1. PRINCIPLES OF PRESENTATION AND ACCOUNTING POLICIES. The consolidated financial statements include the accounts of Georgia-Pacific Corporation and subsidiaries (the "Corporation" or "Georgia-Pacific"). All significant intercompany balances and transactions are eliminated in consolidation. The interim financial information included herein is unaudited; however, such information reflects all adjustments which are, in the opinion of management, necessary for a fair presentation of the Corporation's financial position, results of operations, and cash flows for the interim periods. All such adjustments are of a normal, recurring nature. Certain 2001 amounts have

been reclassified to conform to the 2002 presentation. These consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Corporation's annual report on Form 10-K for the fiscal year ended December 29, 2001.

On December 16, 1997, shareholders of the Corporation approved the creation of two classes of common stock intended to reflect separately the performance of the Corporation's manufacturing and timber businesses. The Corporation's manufacturing and timber businesses are referred to hereinafter as the "Georgia-Pacific Group" and "The Timber Company", respectively. On October 6, 2001, the Corporation completed the spin off of The Timber Company and its merger with and into Plum Creek Timber Company, Inc. ("Plum Creek") (see Note 7). The results of The Timber Company through October 6, 2001 are reported as discontinued operations in the accompanying consolidated financial statements.

The Corporation classifies certain shipping and handling costs as selling and distribution expenses. Shipping and handling costs included in selling and distribution expenses were $143 million and $285 million for the second quarter and first six months of 2002, respectively, and $155 million and $316 for the second quarter and first six months of 2001.

Accounting Changes

In the first quarter of 2002, the Corporation changed its method of computing LIFO inventory increments from year-to-date average cost to latest acquisition cost. The Corporation believes that the latest acquisition cost more closely aligns the value of increases in inventory with physical quantities giving rise to the increases and that this method more appropriately reflects the underlying substance of changes in inventory. In addition, the Corporation changed its method of pooling LIFO inventories from a statutory legal entity approach to an approach that allows the alignment by business segment. The Corporation believes that this approach results in better matching of costs to revenues in a manner that is more consistent with the way the businesses are managed. The cumulative effect of these changes on prior years was not determinable. These changes did not have a material effect on 2002 results of operations or financial position.

Effective December 31, 2000, the Corporation adopted Statement of Financial Accounting Standards ("SFAS") No. 133, "*Accounting for Derivative Instruments and Hedging Activities,"* and, accordingly, all derivatives are recognized on the balance sheet at their fair value. As a result of adopting SFAS 133, the Corporation recorded an after-tax cumulative effect of accounting change credit of $11 million (net of taxes of $6 million) and a $2 million transition adjustment (net of taxes of $1 million) in other comprehensive loss.

Business Separation

On May 7, 2002, the Board of Directors approved separating the Corporation into two public companies. The separation will align the Corporation's businesses into a consumer products and packaging company and a building products and distribution company, each of which will have a distinct strategic focus and competitive strengths and the potential for creation of additional value. The separation is expected to produce a number of other important benefits as well, such as creating both a value-added consumer products and packaging company with strong brands and stable cash flows, and one of the strongest domestic building products companies; providing more focused

employee performance incentives; eliminating cross-subsidies, with each business free to use its cash flow to reinvest or distribute to

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shareholders as appropriate; and allowing each business to adopt its own capital structure. The new consumer products and packaging company will consist of the Corporation's consumer products business, packaging business and pulp and paper business. After the separation, Georgia-Pacific will consist of the Corporation's building products manufacturing and distribution businesses and the Unisource paper distribution business. The Corporation intends to effect the separation through an initial public offering of approximately 15% to 20% of the outstanding shares of the new consumer products and packaging company. The initial public offering is expected to occur in the third quarter of 2002. The Corporation's bondholders will be offered the opportunity to exchange their current Georgia-Pacific Corporation bonds for bonds of the new consumer products and packaging company in a manner that preserves bondholder value. In connection with the separation, new credit facilities will be raised and new long-term bonds will be issued by Georgia-Pacific to repay existing indebtedness. The full separation of the new consumer products and packaging company from Georgia-Pacific is expected to be completed in the first half of 2003 through a tax-free distribution of shares to existing Georgia-Pacific shareholders. The structure and timing of the transactions outlined above are subject to a number of factors, including industry conditions and capital markets.

2. GOODWILL AND INTANGIBLE ASSETS. Effective December 30, 2001, the Corporation adopted SFAS No. 141, *Business Combinations* ("SFAS No. 141"), and SFAS No. 142, *Goodwill and Other Intangible Assets* ("SFAS No. 142"). SFAS No. 141 requires that the purchase method of accounting be used for all business combinations initiated after June 30, 2001. SFAS No. 142 requires that entities assess the fair value of the net assets underlying all acquisition related goodwill on a reporting unit basis effective beginning in 2002. When the fair value is less than the related carrying value, entities are required to reduce the amount of goodwill. The Corporation has determined its reporting units to be the following: structural panels, lumber, industrial wood products, gypsum, chemical, building products distribution, packaging, bleached pulp and paper, paper distribution, North American towel and tissue, Dixie and European consumer products.

The adoption of SFAS No. 142 required the Corporation to perform an initial impairment assessment on all goodwill as of the beginning of 2002 for each of the Corporation's reporting units. In this assessment, the Corporation compared the fair value of the reporting unit to its carrying value. The fair values of the reporting units were calculated based on the present value of future cash flows. The assumptions used in these discounted cash flow analyses were consistent with the reporting unit's internal planning. The cumulative effect of the adoption of this accounting principle was an after-tax charge to earnings of $545 million effective at the beginning of 2002.

The $545 million goodwill impairment related only to the Corporation's Unisource paper distribution reporting unit. The principal facts and circumstances leading to the impairment of the paper distribution reporting unit's goodwill included a diminution of synergies originally expected to be received from the white paper mills sold to Domtar, Inc. in 2001, and changes in the marketplace for coated and uncoated free sheet paper subsequent to the acquisition of Unisource.

On August 13, 2002, the Corporation entered into a letter of intent to sell 60% of its Unisource paper distribution business for approximately $850 million in after-tax proceeds and $170 million of notes receivable. The Corporation will retain a 40% interest in the business. Based on the terms of the letter of intent, the Corporation has concluded that the fair value of this business was further diminished. Accordingly, in the second quarter of 2002, the Corporation recorded an after-tax charge of $170 million which is comprised of an additional goodwill impairment charge of $106 million and a pretax fixed asset impairment charge of $102 million ($64 million after tax) in its bleached pulp and paper segment. Following these impairment charges, the related goodwill has been completely eliminated and fixed assets remaining were approximately $137 million. Once the sale is completed, the Corporation expects to recognize an additional tax benefit of approximately $180 million, which is included in the total after-tax proceeds. The sale is expected to be completed in the fourth quarter of 2002.

In addition, during the second quarter of 2002, the Corporation reclassified goodwill for certain tax liabilities recorded in connection with the Unisource acquisition.

The changes in the carrying amount of goodwill for the first six months of 2002 are as follows:

In millions	Consumer products	Packaging	Bleached pulp and paper	Building products	All other	Consolidated
Balance as of December 29, 2001	$ 6,627	$ 621	$ 975	$ 42	$ -	$ 8,265
Cumulative effect of change in accounting principle - adoption of SFAS No. 142	-	-	(545)	-	-	(545)
Goodwill impairment	-	-	(106)	-	-	(106)
Foreign currency translation	45	-	-	(2)	-	43
Balance sheet reclassifications	-	-	(48)	-	-	(48)
Balance as of June 29, 2002	$ 6,672	$ 621	$ 276	$ 40	$ -	$ 7,609

SFAS No. 142 also requires that entities discontinue amortization of all purchased goodwill, including amortization of goodwill recorded in past business combinations. Accordingly, the Corporation no longer amortized goodwill beginning in 2002. In the first six months of 2001, goodwill amortization expense aggregated $123 million, which included $87 million in the consumer products segment, $11 million in the packaging segment, $24 million in the bleached pulp and paper segment and $1 million in the building products segment. Had the Corporation discontinued amortization of goodwill in the prior year, operating results for the second quarter and first six months of 2001 would have been as follows:

In millions	Second Quarter 2001	First Six Months 2001
Continuing operations:		
Income (loss) from continuing operations, as reported	$ 29	$ (107)
Add back: goodwill amortization	62	123
Adjusted income from continuing operations	$ 91	$ 16
Net income (loss) as reported	$ 29	$ (108)
Add back: goodwill amortization	62	123
Adjusted net income	$ 91	$ 15
Basic and diluted earnings per share:		
Income (loss) from continuing operations, as reported	$ 0.13	$ (0.47)
Add back: goodwill amortization	0.27	0.54
Adjusted income from continuing operations	$ 0.40	$ 0.07
Net income (loss) as reported	$ 0.13	$ (0.48)
Add back: goodwill amortization	0.27	0.54
Adjusted net income	$ 0.40	$ 0.06

Intangible Assets

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

	As of June 29, 2002		As of December 29, 2001	
In millions	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Trademarks	$ 606	$ 23	$ 602	$ 15
Patents and Other	146	27	145	19
Total	$ 752	$ 50	$ 747	$ 34

Aggregate Amortization Expense:

First six months of 2002	$ 15

Estimated Amortization Expense:

For fiscal year 2003	$ 30
For fiscal year 2004	30
For fiscal year 2005	30
For fiscal year 2006	30
For fiscal year 2007	18

The Corporation does not have any intangible assets (other than goodwill) that are not subject to amortization.

3. PROVISION FOR INCOME TAXES. The effective tax rate in 2002 was different than the statutory tax rate primarily because of the write-off of nondeductible goodwill, offset somewhat by lower international effective tax rates and utilization of state tax credits. The effective tax rate in 2001 was different from the statutory rate primarily because of nondeductible goodwill amortization expense associated with business acquisitions.

4. EARNINGS PER SHARE. Basic earnings per share is computed based on net income and the weighted average number of common shares outstanding. Diluted earnings per share reflect the assumed issuance of common shares under long-term incentive stock option and stock purchase plans and pursuant to the terms of the 7.5% Premium Equity Participating Security Units ("PEPS Units"). The computation of diluted earnings per share does not assume conversion or exercise of securities that would have an antidilutive effect on earnings per share.

5. SUPPLEMENTAL DISCLOSURES -- CONSOLIDATED STATEMENTS OF CASH FLOWS. The cash impact of interest and income taxes is reflected in the table below. The effect of foreign currency exchange rate changes on cash was not material in either period.

(In millions)	Six Months Ended 2002	Six Months Ended 2001
Total interest costs	$ 458	$ 603
Interest capitalized	(4)	(4)
Interest expense	$ 454	$ 599
Interest paid	$ 439	$ 628
Income tax paid (refunds received), net	$ 62	$ (31)

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

(In millions)	June 29, 2002	December 29, 2001
Raw materials	$ 570	$ 628
Finished goods	1,530	1,537
Supplies	507	504
LIFO reserve	(101)	(157)
Total inventories	$ 2,506	$ 2,512

7. ACQUISITIONS AND DIVESTITURES. During the first six months of 2002, the Corporation disposed of various assets including a wallboard paper mill for a total of $22 million in cash and recognized a pretax loss of $10 million which was reflected in "Other (income) loss, net" in the accompanying consolidated statements of income. During the first six months of 2001, the

Corporation sold various assets including an industrial wood products property, a lumber mill, a paper distribution business and timberlands for a total of $113 million in cash and recognized a pretax gain of $54 million, $27 million of which was reflected in "Other (income) loss, net" and $27 million of which was reflected in "Income from discontinued operation, net of taxes" in the accompanying consolidated statements of income.

During the first quarter of 2001, the Corporation acquired the remaining ownership of two chemical joint ventures for approximately $26 million. The results of operations of these chemical businesses were consolidated with those of the Corporation beginning in February 2001. The Corporation has accounted for these acquisitions using the purchase method to record a new cost basis for assets acquired and liabilities assumed.

Pursuant to a consent decree executed with the United States Department of Justice in connection with the 2000 acquisition of the Fort James Corporation, the Corporation sold a portion of its away-from-home tissue manufacturing assets (formerly Georgia-Pacific Tissue) to Svenska Cellulosa Aktiebolaget (publ) for approximately $850 million. The sale was completed on March 2, 2001, with net proceeds of approximately $581 million ($660 million after tax benefit) used to repay debt. In the fourth quarter of 2000, the Corporation recorded a pretax loss of $204 million in the consumer products segment for the write-down of these assets to their net realizable value; accordingly, no significant gain or loss was recognized upon completion of the sale in 2001.

On October 6, 2001, the Corporation completed the spin off of The Timber Company and its merger with and into Plum Creek. In accordance with the merger agreement, shareholders of The Timber Company received 1.37 shares of Plum Creek stock for each share of The Timber Company stock. This transaction, which included the assumption by Plum Creek of $646 million of the Corporation's debt, was valued at approximately $3.4 billion. Plum Creek assumed a 10-year timber supply agreement between the Corporation and The Timber Company.

The transaction was originally conditioned on the receipt of a private letter ruling from the Internal Revenue Service (the "Service") that the transaction would be tax-free to the Corporation and to the shareholders of The Timber Company. In June 2001, the Corporation and Plum Creek amended the original merger agreement and determined to effect the merger upon receipt of opinions from tax counsel that the spin off of The Timber Company from the Corporation and the subsequent merger with Plum Creek would be tax-free to the Corporation and to the shareholders of The Timber Company. The Service notified the companies on June 12, 2001, that it had decided not to issue the private letter ruling based on its belief that the companies had failed to carry the high burden of proof of business purpose necessary for the transaction to receive such an advance ruling. This high burden of proof, which is more stringent than the legal standards applicable to the audit process or any judicial proceeding, pertains only to advance rulings. Based on discussion with the Service and the advice of legal counsel, the companies believe the transaction will not be taxable to the Corporation or the shareholders of The Timber Company. As an added measure to reduce the uncertainty concerning any possible tax risks associated with the transaction, the Corporation obtained up to $500 million in tax liability insurance.

The Timber Company has been treated as a discontinued operation in the accompanying consolidated financial statements. Operating results of the discontinued operation were as follows:

In millions	Second Quarter 2001	Six Months Ended 2001
Net sales	$ 89	$ 180
Income before income taxes	$ 57	$ 93
Provision for income taxes	(21)	(35)
Income from discontinued operation	$ 36	$ 58

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8. RESTRUCTURING. In connection with the acquisition of Fort James, the Corporation recorded liabilities totaling approximately $78 million for employee termination costs relating to approximately 960 hourly and salaried employees. In addition, the Corporation determined that it would strategically reposition its communication papers business to focus on faster-growing paper segments by retiring four high-cost paper machines and associated pulping facilities at its Camas Washington mill and recorded liabilities of approximately $26 million to exit these activities. In addition, the Corporation recorded liabilities of $35 million primarily for lease and contract termination costs at administrative facilities that have been or will be closed in California, Connecticut, Illinois, Virginia and Wisconsin. During 2001, approximately 605 employees were terminated and approximately $55 million of the reserve was used to pay termination benefits. During 2002, approximately 112 employees were terminated and approximately $10 million of the reserve was used to pay termination benefits. The remaining employee terminations and Camas facility closing activities (primarily demolition activities) are expected to be completed early in 2003. The leases and contracts at the administrative facilities expire through 2012. The following table provides a rollforward of these reserves from December 29, 2001 through June 29, 2002:

Type of Cost In millions	Liability Balance at December 29, 2001	Use	Liability Balance at June 29, 2002
Employee termination	$ 23	$ (10)	$ 13
Facility closing costs	58	(10)	48
Total	$ 81	$ (20)	$ 61

On March 30, 2001, the Corporation announced that it would permanently close its pulp mill and associated chemical plant at Bellingham, Washington. This decision was based on the age of the facility and the extraordinarily high energy costs on the West Coast in late 2000. These operations had been temporarily closed since December 2000. The Bellingham pulp mill produced approximately 220,000 tons of pulp, including 135,000 tons of sulfite market pulp, and 260,000 tons of lignin annually. In connection with this closure the Corporation recorded a pretax charge to earnings in the consumer products segment of approximately $57 million for the write-off and impairment of assets, approximately $13 million for the termination of approximately 420 hourly and salaried employees and approximately $12 million for facility closing costs. Of the $82 million total pretax charge to earnings, $78 million was charged to cost of sales, $3 million was charged to selling and distribution expense and $1 million was charged to general and administrative expenses. The carrying value of the assets for which the impairment was recorded, subsequent to the write down, was approximately $5 million at March 30, 2001. During 2001, 410 employees were terminated and all of the employee termination reserve was used to pay termination benefits.

In connection with overall weak market conditions in the wallboard market due to excess capacity in the industry, the Corporation announced in June 2001 that it would close gypsum wallboard plants at Savannah, Georgia; Long Beach, California; and Winnipeg, Manitoba, Canada. The Corporation also announced that it would indefinitely idle wallboard production lines at Acme, Texas; Sigurd, Utah; and Blue Rapids, Kansas; and reduce operations at its remaining gypsum wallboard production facilities. The plant closures and production curtailments affect approximately 45% of the Corporation's gypsum wallboard production capacity. In connection with this announcement, the Corporation recorded a pretax charge to earnings in the building products segment of approximately $57 million for the write-off and impairment of assets, approximately $5 million for the termination of approximately 350 hourly and salaried employees, and approximately $5 million for facility closing costs, most of which was charged to cost of sales. The fair value of impaired assets was determined using the present value of expected future cash flows or the expected net realizable value. The carrying value of the assets for which the impairment was recorded, subsequent to the write down, was approximately $35 million at June 2001. During 2001, 234 employees were terminated and approximately $3 million of the reserve was used to pay termination benefits.

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9. DEBT. The Corporation's total debt, excluding senior deferrable notes, decreased to $12,086 million at June 29, 2002 from $12,214 million at December 29, 2001. At June 29, 2002, the weighted average interest rate on the Corporation's total debt, excluding senior deferrable notes and including outstanding interest rate exchange agreements was 6.38%.

The Corporation had commitments totaling $1.3 billion and CN $95 million (approximately $63 million) under its United States and Canadian accounts receivable secured borrowing programs, respectively, of which $1.3 billion and CN $95 million was outstanding under these programs at June 29, 2002. Of the $1.3 billion in the United States program, $395 million will expire in September 2002 and the remaining $900 million expires in December 2002. The Canadian program expires in May 2004. The Corporation expects to renew these agreements prior to expiration. The receivables outstanding under these programs and the corresponding debt are included as "Receivables" and "Commercial paper and other short-term notes," respectively, on the accompanying consolidated balance sheets. All accounts receivable programs are accounted for as secured borrowings. As collections reduce previously pledged interests, new receivables may be pledged.

On April 27, 2002, the Corporation issued $73 million of its variable rate industrial revenue bonds, due February 1, 2022 to replace the maturity of $73 million of its variable rate industrial revenue bonds. On June 15, 2002, $300 million of the Corporation's 9.95% debentures matured.

At June 29, 2002, the Corporation's unsecured financing facility totaled $850 million with a maturity date of August 16, 2002 and the unsecured revolving credit facility totaled $3,750 million with a maturity date of November 3, 2005. Borrowings under the agreements bear interest at market rates. These interest rates may be adjusted according to a rate grid based on the Corporation's long-term debt ratings. Fees associated with these revolving credit facilities include a facility fee of 0.2% per annum on the aggregate commitments of the lenders as well as up-front fees. During the first six months of 2002, the Corporation paid $4 million in facility fees. Fees and margins may also be adjusted according to a pricing grid based on the Corporation's long-term debt ratings. At June 29, 2002, $3,429 million was borrowed under the credit agreements at a weighted-average interest rate of 3.1%. Amounts outstanding under the revolving credit facilities are included in "Commercial paper and other short-term notes" and "Long-term debt, excluding current portion" on the accompanying consolidated balance sheets.

The Corporation's amounts outstanding under the credit agreements include the following:

In millions	June 29, 2002
Commitments:	
Multi-Year Revolving Credit Facility	$ 3,750
Capital Markets Bridge Facility	850
Credit facilities available	4,600
Amounts Outstanding:	
Letter of Credit Agreements**	(399)
Multi-Year Revolving Credit Facility due November 2005, average rate of 3.47%	(2,180)
Capital Markets Bridge Facility due August 2002, average rate of 3.59%	(850)
Total credit balance	(3,429)
Total credit available*	$ 1,171

* At June 29, 2002, the Corporation was limited to $979 million of incremental debt available pursuant to certain restrictive debt covenants and its outstanding debt balance at June 29, 2002. This limitation on available credit will be reduced as the Corporation pays down debt.

** The Letter of Credit Agreements only include Standby Letters of Credit.

The unsecured financing facilities require a maximum leverage ratio (funded indebtedness, excluding senior deferrable notes, to net worth plus funded indebtedness) of 72.50% on June 29, 2002; 70.00% on September 28, 2002, December 28, 2002 and March 29, 2003; 67.50% on June 28, 2003 and September 27, 2003; and 65.00% on January 3, 2004 and thereafter. The restrictive covenants also require a minimum interest coverage ratio (earnings before interest, taxes, depreciation and amortization, "EBITDA", to interest charges) of 2.25 to 1.00 on June 29, 2002 and September 28, 2002; 2.50 to 1.00 on December 28, 2002 and March 29, 2003; 2.75 to 1.00 on June 28, 2003 and September 27, 2003; and 3.00 to 1.00 on January 3, 2004 and thereafter. In addition, the restrictive covenants require a minimum net worth that changes quarterly and a maximum debt level of $13,065 million. The Corporation was in compliance with these debt covenants as of June 29, 2002 with a leverage ratio of 70.70%, an interest coverage ratio of 2.81 to 1.00, and a debt balance of $12,086 million.

At June 29, 2002, the Corporation had interest rate exchange agreements that effectively converted $1,441 million of floating rate obligations with a weighted average interest rate of 1.95% to fixed rate obligations with an average effective interest rate of approximately 5.87%. These agreements increased interest expense by $30 million during the first six months of 2002. The agreements had a weighted-average maturity of approximately four months at June 29, 2002.

At June 29, 2002, the Corporation also had interest rate exchange agreements (a collar) that effectively capped $47 million of floating rate obligations to a maximum interest rate of 7.5% and established a minimum interest rate on such obligations of 5.5%. The Corporation's interest expense is unaffected by this agreement when the market interest rate falls within this range. This agreement reduced interest expense by $1.2 million during the first six months of 2002. The agreement had a weighted-average maturity of approximately three years at June 29, 2002.

The estimated fair value of the Corporation's interest rate exchange agreements at June 29, 2002 was a $17 million liability. The liability balance represents the estimated amount the Corporation would have to pay to terminate the agreements. The fair value at June 29, 2002 was estimated by calculating the present value of anticipated cash flows. The discount rate used was an estimated borrowing rate for similar debt instruments with like maturities.

As of June 29, 2002, the Corporation had $1.5 billion of debt and equity securities available for issuance under a shelf registration statement filed with the Securities and Exchange Commission during fiscal year 2000.

The Corporation's borrowing arrangements contain a number of financial and non-financial covenants, which restrict the activities of the Corporation. The more significant financial covenants are discussed above. In addition, certain agreements contain cross-default provisions. The Corporation is in compliance with the covenants of these agreements.

On May 8, 2002, Moody's Investor Service changed the Corporation's unsecured debt rating to "Ba1" from "Baa3", and its commercial paper rating to "Not-Prime" from "Prime-3".

On August 7, 2002, the Corporation announced that it obtained a $650 million bridge financing commitment from Bank of America, N.A. and Goldman Sachs Credit Partners, L.P. This bridge loan, along with the available cash and borrowings from existing bank credit facilities, will be used to repay $850 million in bridge financing due August 16, 2002. Under the terms of this commitment, the lenders have the right to cause the Corporation to repay or refinance this bridge loan in full on the earlier of February 16, 2003 or forty-five days after the Corporation terminates the transactions described in Note 1 -- *Business Separation* above. If the Corporation does not make other financing arrangements satisfactory to the lenders, they have the right to arrange and manage the financing necessary for such repayment or refinancing, which would be secured by a first lien on the receivables and inventory of the Corporation and its subsidiaries to the extent permitted by the Corporation's other financing arrangements.

10. SENIOR DEFERRABLE NOTES. In July 1999, the Corporation issued 17,250,000 of 7.5% PEPS Units for $862.5 million. Each PEPS Unit consists of a purchase contract that obligates the holder to purchase shares of Georgia-Pacific common stock for $50 on or prior to August 16, 2002 and a senior deferrable note of the Corporation due August 16, 2004. The amount of shares purchased per PEPS Unit will be based on the average closing price of Georgia-Pacific common stock over a 20-day trading period ending August 13, 2002. Assuming an average stock price of less than $47.375 per share, the Corporation expects to issue approximately 18.2 million shares of Georgia-Pacific common stock in 2002. Each purchase contract yields interest of 0.35% per year, paid quarterly, on the $50 stated amount of the PEPS Unit. Each senior deferrable note yields interest of 7.15% per year, paid quarterly, until August 16, 2002. The terms of the PEPS offering included a remarketing of the senior deferrable notes on August 16, 2002. On August 7, 2002, the Corporation announced that the senior deferrable notes would not be remarketed. The liability related to the PEPS Units is classified as "Senior deferrable notes" on the accompanying consolidated balance sheets.

11. DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES. Effective December 31, 2000, the Corporation adopted Statement of Financial Accounting Standards No. 133, "*Accounting for Derivative Instruments and Hedging Activities,"* and, accordingly, all derivatives are recognized on the balance sheet at their fair value.

The Corporation formally documents all relations between hedging instruments and the hedged items, as well as its risk-management objectives and strategy for undertaking various hedge transactions. The Corporation formally assesses, both at the hedge's inception and on an ongoing basis, whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in cash flows of the hedged items.

Cash Flow Hedges

: The Corporation uses interest rate agreements in the normal course of business to manage and reduce the risk inherent in interest rate fluctuations. Interest rate swap agreements are considered hedges of specific borrowings and differences paid and received under the swap arrangements are recognized as adjustments to interest expense. Such contracts had a total notional amount of $1.3

billion at June 29, 2002. The fair market value of such contracts was a liability of $15 million at June 29, 2002.

With each type of cash flow hedge, the settlement of the forecasted transaction will result in the reclassification into earnings of gains and losses that are reported in accumulated other comprehensive loss. As of June 29, 2002, approximately $18 million of deferred losses on derivative instruments included in accumulated other comprehensive loss are expected to be reclassified to earnings during the next twelve months. These losses are primarily related to the floating-to-fixed interest rate swap agreements and are due to the significant decrease in interest rates during the contract terms.

Hedge of the net investment in a foreign operation:

At June 29, 2002, the Corporation had outstanding approximately $273 million (net of discount) of Euro-denominated bonds which were designated as a hedge against its net investment in Europe.

Non-designated/ineffective derivative instruments:

The Corporation has two foreign currency interest rate swap agreements that were assumed in the acquisition of Fort James. These agreements do not qualify for hedge accounting. Included in the cumulative effect of accounting change is a pre-tax loss of $1 million relating to the fair value of these agreements. The fair value of these agreements at June 29, 2002 was a liability of approximately $1 million. The Corporation also has three interest rate swaps that, during the third quarter of 2001, were no longer highly effective in offsetting changes in cash flows of the borrowings hedged. The notional amount of these instruments was $127 million. At June 29, 2002, the fair market value of these three instruments was a liability of approximately $2 million.

During 2000, the Corporation entered into a derivative agreement in connection with the sale of certain packaging assets whereby the Corporation has guaranteed a certain margin on the buyer's production. This derivative agreement expires in 2005. This agreement does not qualify for hedge accounting because the buyer's production does not qualify as a hedged item in accordance with SFAS No. 133. The Corporation also entered into certain commodity swap agreements to offset the gain on the aforementioned derivative agreement. The net fair value of these derivative agreements was $17.3 million (pre-tax) at December 30, 2000 and is included in the cumulative effect of accounting change. Effective December 28, 2001, the Corporation terminated the offsetting commodity agreements. The termination was effective with the counter-party's bankruptcy filing. As of June 29, 2002, the fair market value of the original derivative agreement was an asset of $9.1 million.

The Corporation's senior management establishes the parameters of the Corporation's financial risk, which have been approved by the Board of Directors. Hedging interest rate exposure through the use of swaps and options and hedging foreign exchange exposure through the use of forward contracts are specifically contemplated to manage risk in keeping with management's policy. Derivative instruments, such as swaps, forwards, options or futures, which are based directly or indirectly upon interest rates, currencies, equities and commodities, may be used by the Corporation to manage and reduce the risk inherent in price, currency and interest rate fluctuations.

The Corporation does not utilize derivatives for speculative purposes. Derivatives are transaction-specific so that a specific debt instrument, contract or invoice determines the amount, maturity and other specifics of the hedge. Counterparty risk is limited to institutions with long-term debt ratings of A or better.

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12. LONG-TERM APPRECIATION PLAN. In 2001 the Corporation began granting stock appreciation rights ("SAR") for issuance under the 2001 Long-Term Appreciation Plan (the "LTAP"). The LTAP provides for the granting of SAR units to key employees of the Corporation. During the first six months of both 2002 and 2001, the Corporation granted 2.4 million SAR units under the LTAP with an exercise price of $24.44 per unit in 2002 and $29.47 per unit in 2001, respectively. The SAR exercise price was based on the underlying fair value of Georgia-Pacific Group common stock at the grant date. These SAR units vest over three years. Compensation expense for the SARs is based on the difference between the current fair market value of Georgia-Pacific Group common stock and the fair market value at the date of grant. During the second quarter and first six months of 2002 the Corporation did not record compensation expense related to these SARs. During the second quarter and first six months of 2001, the Corporation recorded compensation expense of $3 million.

13. COMMITMENTS AND CONTINGENCIES.

ENVIRONMENTAL MATTERS

The Corporation is a party to various legal proceedings incidental to its business and is subject to a variety of environmental and pollution control laws and regulations in all jurisdictions in which it operates. As is the case with other companies in similar industries, the Corporation faces exposure from actual or potential claims and legal proceedings involving environmental matters. Liability insurance in effect during the last several years provides only very limited coverage for environmental matters.

The Corporation is involved in environmental remediation activities at approximately 169 sites, both owned by the Corporation and owned by others, where it has been notified that it is or may be a potentially responsible party ("PRP") under the United States Comprehensive Environmental Response, Compensation and Liability Act ("CERCLA") or similar state "superfund" laws. Of the known sites in which it is involved, the Corporation estimates that approximately 36% are being investigated, approximately 21% are being remediated and approximately 43% are being monitored (an activity that occurs after either site investigation or remediation has been completed). The ultimate costs to the Corporation for the investigation, remediation and monitoring of many of these sites cannot be predicted with certainty, due to the often unknown nature and magnitude of the pollution or the necessary cleanup, the varying costs of alternative cleanup methods, the amount of time necessary to accomplish such cleanups, the evolving nature of cleanup technologies and governmental regulations, and the inability to determine the Corporation's share of multiparty cleanups or the extent to which contribution will be available from other parties, all of which factors are taken into account to the extent possible in estimating the Corporation's liabilities. The Corporation has established reserves for environmental remediation costs for these sites that it

believes are probable and reasonably able to be estimated. To the extent that the Corporation is aware of unasserted claims, considers them probable, and can estimate their potential costs, the Corporation includes appropriate amounts in the reserves.

Based on analyses of currently available information and previous experience with respect to the cleanup of hazardous substances, the Corporation believes it is reasonably possible that costs associated with these sites may exceed current reserves by amounts that may prove insignificant or that could range, in the aggregate, up to approximately $122 million. This estimate of the range of reasonably possible additional costs is less certain than the estimates upon which reserves are based, and in order to establish the upper limit of such range, assumptions least favorable to the Corporation among the range of reasonably possible outcomes were used. In estimating both its current reserve for environmental remediation and the possible range of additional costs, the Corporation has not assumed it will bear the entire cost of remediation of every site to the exclusion of other known PRPs who may be jointly and severally liable. The ability of other PRPs to participate has been taken into account, based generally on their financial condition and probable contribution on a per-site basis.

Presented below is the activity in the Corporation's environmental liability account for the last three fiscal years and first half of 2002.

In millions	First Six Months	Fiscal Year Ended		
	2002	2001	2000	1999
Beginning balance	$ 308	$ 120	$ 57	$ 47
Expense charged to earnings:				
Related to previously existing matters	12	2	29	22
Related to new matters	-	-	1	3
Amounts related to acquisitions/(divestitures):				
Amounts assumed by others in divestitures	-	-	-	-
Original purchase price allocations	-	-	49	1
Changes in allocation of purchase price	-	207	-	-
Payments	(8)	(21)	(16)	(16)
Ending balance	$ 312	$ 308	$ 120	$ 57

Expense charged to earnings in the above table includes amounts accrued for new matters and changes in existing estimates. Payments represent amounts paid in full or partial settlement or for environmental studies and similar costs.

KALAMAZOO RIVER SUPERFUND SITE

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