

POTLATCH CORP
Form 10-Q
April 23, 2014

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

Form 10-Q

(Mark One)

Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the quarterly period ended March 31, 2014

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 1-32729

POTLATCH CORPORATION
(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization) 601 West First Avenue, Suite 1600 Spokane, Washington (Address of principal executive offices) (509) 835-1500 (Registrant's telephone number, including area code)	82-0156045 (I.R.S. Employer Identification No.) 99201 (Zip Code)
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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 and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted 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 and post such files). Yes No

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

Large accelerated filer	<input checked="" type="checkbox"/>	Accelerated filer	<input type="checkbox"/>
Non-accelerated filer	<input type="checkbox"/>	Smaller reporting company	<input type="checkbox"/>

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

The number of shares of common stock of the registrant outstanding as of April 21, 2014 was 40,590,655.

POTLATCH CORPORATION AND CONSOLIDATED SUBSIDIARIES

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Part I

ITEM 1. FINANCIAL STATEMENTS

Potlatch Corporation and Consolidated Subsidiaries

Consolidated Statements of Income

Unaudited (Dollars in thousands, except per-share amounts)

	Three Months Ended	
	March 31,	
	2014	2013
Revenues	\$139,579	\$139,253
Costs and expenses:		
Cost of goods sold	98,593	98,299
Selling, general and administrative expenses	9,677	13,596
Environmental remediation charge	—	750
	108,270	112,645
Operating income	31,309	26,608
Interest expense, net	(5,460	) (6,336
Income before income taxes	25,849	20,272
Income tax provision	(5,499	) (4,785
Net income	\$20,350	\$15,487
Net income per share:		
Basic	\$0.50	\$0.38
Diluted	0.50	0.38
Distributions per share	\$0.35	\$0.31
Weighted average shares outstanding (in thousands):		
Basic	40,561	40,436
Diluted	40,682	40,613

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

Potlatch Corporation and Consolidated Subsidiaries
 Consolidated Statements of Comprehensive Income
 Unaudited (Dollars in thousands)

	Three Months Ended March 31,	
	2014	2013
Net income	\$20,350	\$15,487
Other comprehensive income, net of tax:		
Defined benefit pension plans and other postretirement employee benefits:		
Amortization of prior service credit included in net periodic cost, net of tax of \$(867) and \$(870)	(1,356	) (1,362
Amortization of actuarial loss included in net periodic cost, net of tax of \$1,677 and \$2,246	2,622	3,513
Other comprehensive income, net of tax	1,266	2,151
Comprehensive income	\$21,616	\$17,638

Amortization of prior service credit and amortization of actuarial loss are included in the computation of net periodic cost. See [Note 6: Pension Plans and Other Postretirement Employee Benefits](#) for additional information.

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

Potlatch Corporation and Consolidated Subsidiaries
Consolidated Condensed Balance Sheets
Unaudited (Dollars in thousands, except per-share amounts)

	March 31, 2014	December 31, 2013
ASSETS		
Current assets:		
Cash	\$9,364	\$5,586
Short-term investments	66,950	52,251
Receivables, net	12,593	16,572
Inventories	34,231	36,275
Deferred tax assets	7,724	7,724
Other assets	8,239	11,961
Total current assets	139,101	130,369
Property, plant and equipment, net	60,071	59,976
Timber and timberlands, net	451,109	455,871
Deferred tax assets	20,833	21,576
Other assets	12,766	12,738
Total assets	\$683,880	\$680,530
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Current installments on long-term debt	\$—	\$—
Accounts payable and accrued liabilities	49,462	50,318
Total current liabilities	49,462	50,318
Long-term debt	320,014	320,092
Liability for pensions and other postretirement employee benefits	82,448	83,619
Other long-term obligations	20,658	22,353
Stockholders' equity	211,298	204,148
Total liabilities and stockholders' equity	\$683,880	\$680,530
Shares outstanding (in thousands)	40,589	40,537
Working capital	\$89,639	\$80,051
Current ratio	2.8:1	2.6:1

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

Potlatch Corporation and Consolidated Subsidiaries
Consolidated Condensed Statements of Cash Flows
Unaudited (Dollars in thousands)

	Three Months Ended March 31,	
	2014	2013
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	\$20,350	\$15,487
Adjustments to reconcile net income to net cash from operating activities:		
Depreciation, depletion and amortization	6,104	6,867
Basis of real estate sold	4,622	457
Change in deferred taxes	(164	) 215
Employee benefit plans	(178	) 2,799
Employee equity-based compensation expense	908	1,072
Other, net	(581	) (41
Working capital and operating related activities	8,923	1,078
Net cash from operating activities	39,984	27,934
CASH FLOWS FROM INVESTING ACTIVITIES		
Change in short-term investments	(14,699	) 7,639
Additions to property, plant and equipment	(2,168	) (2,321
Additions to timber and timberlands	(1,469	) (2,311
Other, net	108	(373
Net cash from investing activities	(18,228	) 2,634
CASH FLOWS FROM FINANCING ACTIVITIES		
Distributions to common stockholders	(14,206	) (12,552
Repayment of long-term debt	—	(27,650
Issuance of common stock	—	667
Employee tax withholdings on equity-based compensation	(1,068	) (1,685
Change in book overdrafts	(2,636	) (2,030
Other, net	(68	) (24
Net cash from financing activities	(17,978	) (43,274
Change in cash	3,778	(12,706
Cash at beginning of period	5,586	16,985
Cash at end of period	\$9,364	\$4,279
SUPPLEMENTAL CASH FLOW INFORMATION		
Cash paid during the period for:		
Interest, net of amount capitalized	\$693	\$1,550
Income taxes, net	11	112

Certain 2013 amounts have been reclassified to conform to the 2014 presentation.

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

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NOTE 1. BASIS OF PRESENTATION

For purposes of this report, any reference to “Potlatch,” “the company,” “we,” “us,” and “our” means Potlatch Corporation and all of its wholly owned subsidiaries, except where the context indicates otherwise.

The accompanying unaudited consolidated financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission pertaining to interim financial statements; certain disclosures normally provided in accordance with generally accepted accounting principles in the United States have been omitted. This Quarterly Report on Form 10-Q should be read in conjunction with our Annual Report on Form 10-K for the year ended December 31, 2013, as filed with the Securities and Exchange Commission on February 14, 2014. We believe that all adjustments necessary for a fair statement of the results of such interim periods have been included.

NOTE 2. INCOME TAXES

As a real estate investment trust (REIT), we generally are not subject to federal and state corporate income taxes on income of the REIT that we distribute to our shareholders. We are, however, subject to corporate taxes on built-in gains (the excess of fair market value over tax basis on January 1, 2006) on sales of real property held by the REIT during the first ten years following the REIT conversion. The sale of standing timber is not subject to built-in gains tax. The Small Business Jobs Act of 2010 modified the built-in gains provisions to exempt sales of real properties in 2011, if five years of the recognition period had elapsed before January 1, 2011. The American Taxpayer Relief Act of 2012 extended the reduced five-year holding period for sales occurring in 2012 and 2013. Accordingly, the built-in gains tax did not apply to sales of real property that occurred in 2011, 2012 and 2013.

We conduct certain activities through our taxable REIT subsidiaries (TRS), which are subject to corporate level federal and state income taxes. These activities are principally comprised of our wood products manufacturing operations and certain real estate investments held for development and resale.

For the three months ended March 31, 2014 and 2013, we recorded income tax provisions of \$5.5 million and \$4.8 million, respectively, primarily due to pre-tax income of the TRS.

NOTE 3. EARNINGS PER SHARE

The following table reconciles the number of shares used in calculating the basic and diluted earnings per share for the three months ended March 31:

(Dollars in thousands, except per-share amounts)	Three Months Ended	
	March 31,	
	2014	2013
Net income	\$20,350	\$15,487
Basic weighted average shares outstanding	40,561,017	40,435,608
Incremental shares due to:		
Performance shares	60,517	95,523
Restricted stock units	57,740	63,607
Stock options	2,834	18,236
Diluted weighted average shares outstanding	40,682,108	40,612,974
Basic net income per share	\$0.50	\$0.38
Diluted net income per share	\$0.50	\$0.38
Antidilutive shares excluded from the calculation:		
Performance shares	69,054	64,905
Restricted stock units	—	4,264
Total antidilutive shares excluded from the calculation	69,054	69,169

NOTE 4. EQUITY-BASED COMPENSATION

As of March 31, 2014, we had three stock incentive plans under which performance share grants, restricted stock unit (RSU) grants and stock options were outstanding, with approximately 196,000 shares authorized for future use under the 2005 Stock Incentive Plan.

The following table details our equity-based compensation expense and director deferred compensation expense for the three months ended March 31:

(Dollars in thousands)	Three Months Ended	
	March 31,	
	2014	2013
Employee equity-based compensation expense:		
Performance shares	\$734	\$862
Restricted stock units	174	210
Total employee equity-based compensation expense	\$908	\$1,072
Total tax benefit recognized from equity-based plans	\$74	\$76
Director deferred compensation (income) expense	\$(441	) \$1,290

PERFORMANCE SHARES

The following table presents the key inputs used in the Monte Carlo simulation method to calculate the fair value of the performance share awards in 2014 and 2013, and the resulting fair values:

	2014	2013		
Shares granted	87,441	83,111		
Stock price as of valuation date	\$39.76	\$45.31		
Risk-free rate	0.72	% 0.40	%	%
Fair value of a performance share	\$45.57	\$62.78		

The following table summarizes outstanding performance share awards as of March 31, 2014, and changes during the three months ended March 31, 2014:

(Dollars in thousands, except grant date fair value)	Shares	Weighted Avg. Grant Date Fair Value	Aggregate Intrinsic Value
Unvested shares outstanding at January 1	155,814	\$48.73	
Granted	87,441	45.57	
Forfeited	—	—	
Unvested shares outstanding at March 31	243,255	47.60	\$9,412

As of March 31, 2014, there was \$7.2 million of unrecognized compensation cost related to unvested performance share awards, which is expected to be recognized over a weighted average period of 1.8 years.

RESTRICTED STOCK UNITS

The following table summarizes outstanding RSU awards as of March 31, 2014, and changes during the three months ended March 31, 2014:

(Dollars in thousands, except grant date fair value)	Shares	Weighted Avg. Grant Date Fair Value	Aggregate Intrinsic Value
Unvested shares outstanding at January 1			