SCHWEITZER MAUDUIT INTERNATIONAL INC
Form 10-K
February 28, 2014

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

FORM 10-K
(Mark One)

x ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2013

OR

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from __________________ to __________________

1-13948
(Commission file number)

SCHWEITZER-MAUDUIT INTERNATIONAL, INC.
(Exact name of registrant as specified in its charter)

Delaware	62-1612879
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
100 North Point Center East, Suite 600 Alpharetta, Georgia	30022
(Address of principal executive offices)	(Zip Code)

1-800-514-0186
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common stock, par value $0.10 per share (together with associated preferred stock purchase rights)	New York Stock Exchange

Securities Registered Pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes x No o
Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes o No x
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 x No o
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 x No o
Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information

statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. x
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. (Check one):

Large accelerated filer x	Accelerated filer o	Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

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

The aggregate market value of the outstanding common stock, par value $0.10 per share (the “Common Stock”), held by non-affiliates of the registrant as of June 28, 2013 (the last business day of the registrant's most recently completed second fiscal quarter) was $1.5 billion, based on the last sale price for the Common Stock of $49.88 per share as reported on the New York Stock Exchange on said date. For purposes of the foregoing sentence only, all directors and executive officers are assumed to be affiliates.

There were 30,399,784 shares of Common Stock issued and outstanding as of February 26, 2014.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's definitive Proxy Statement relating to its 2014 Annual Meeting of Stockholders scheduled to be held on April 24, 2014 (the "2014 Proxy Statement") and filed pursuant to Regulation 14A are incorporated by reference into Part III of this Annual Report on Form 10-K.

SCHWEITZER-MAUDUIT INTERNATIONAL, INC.

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PART I.
Item 1. Business

GENERAL

Schweitzer-Mauduit International, Inc. (referred to, with its consolidated subsidiaries, as "we", "us", "our", the "Company", "SWM INTL" or "SWM" unless the context indicates otherwise) is a multinational diversified producer of premium specialty papers and resin-based products headquartered in the United States of America.

The Company was incorporated in Delaware in 1995 as a wholly-owned subsidiary of Kimberly-Clark Corporation ("Kimberly-Clark"). On November 30, 1995, Kimberly-Clark distributed its tobacco-related paper and other specialty paper products businesses conducted in the United States, France and Canada to the Company, through a distribution to Kimberly-Clark stockholders of all of the outstanding shares of common stock of the Company (the "spin-off"). Today, we manufacture and sell paper and reconstituted tobacco products to the tobacco industry as well as specialized paper products for use in other applications. We manufacture lightweight specialty papers, which are used in manufacturing ventilated cigarettes, and banded papers for the production of lower ignition propensity, or LIP, cigarettes and are the leading independent producer of reconstituted tobacco leaf, or RTL, used in producing blended cigarettes. We also manufacture resin-based plastic netting through an extrusion process, as well as certain meltblown products and machined plastic core tubes.

Tobacco industry products comprised approximately 93% to 94% of our consolidated net sales in each of the years 2011 through 2013. Our primary products sold to the tobacco industry include cigarette, plug wrap and base tipping papers, or Cigarette Papers, used to wrap various parts of a cigarette and RTL, which is used as a blend with virgin tobacco in cigarettes, reconstituted tobacco wrappers and binders for cigars. These products are sold directly to the major tobacco companies or their designated converters in the Americas, Europe, Asia and elsewhere. Our non-tobacco industry products are a diverse mix of products that includes low volume, high-value engineered papers and, commodity paper grades produced to maximize our machine utilization. In 2013, we acquired DelStar, Inc. ("DelStar"), a manufacturer of plastic netting and other resin-based products focused on the filtration and medical markets.

We conduct business in over 90 countries and operate 14 production locations worldwide, with facilities in the United States, Canada, France, Brazil, China and Poland. We also have a 50% equity interest in two joint ventures in China. The first, China Tobacco Mauduit (Jiangmen) Paper Industry Ltd., or CTM, produces cigarette and porous plug wrap papers and the second, whose facility is under construction, China Tobacco Schweitzer (Yunnan) Reconstituted Tobacco Co. Ltd., or CTS, will produce RTL.

Our wholly-owned, majority-owned and controlled subsidiaries are as follows: Schweitzer-Mauduit Canada, Inc., or SM-Canada; Schweitzer-Mauduit Spain, S.L., or SM-Spain, a holding company organized under the Spanish holding company regime and the primary foreign investment holding company for SWM; SWM RTL Philippines Inc. or RTLP; SWM Luxembourg S.à.r.l, or SWM Lux, a holding company incorporated in Luxembourg; SWM HoldCo 1 S à.r.l., or HoldCo 1, a holding company incorporated in Luxembourg, SWM HoldCo 2 S.à.r.l or HoldCo 2, a holding company incorporated in Luxembourg, SWM Acquisition Corp. I, or Acquisition Corp I, a holding company incorporated in Delaware and Schweitzer-Mauduit International China, Limited, or SM-China, a holding company incorporated in Hong Kong. SM-China owns 50% of the equity interest in CTM, a Sino-Foreign Equity Joint Venture with China National Tobacco Corporation, or CNTC, that manufactures and sells tobacco-related papers in China and 50% of the equity interest in CTS, a Sino-Foreign Equity Joint Venture with CNTC that will manufacture RTL. Both CTM and CTS are unconsolidated subsidiaries. We indirectly through SM-Spain have subsidiaries in France and the Philippines. SM-Spain owns directly 100% of Schweitzer-Mauduit Holding S.A.S., a French holding company, or SMH, and SMH owns 100% of Schweitzer-Mauduit Industries S.A.S., a French corporation, or SMI. Schweitzer-Mauduit International, Inc., SMH and SMI together own 100% of a second holding company,

Schweitzer-Mauduit France S.A.S., a French corporation, or SMF, which holds our French paper operations. SMF directly owns 100% of Schweitzer-Mauduit Developpements S.A.S., a French corporation, or SMD, and SMD owns 100% of LTR Industries S.A.S., a French corporation, or LTRI, our French RTL operation. SMF directly owns 100% of two principal French operating subsidiaries, SWM Services S.A.S. (formerly known as Papeteries de Mauduit S.A.S.), or SWM-S, and Papeteries de

Saint-Girons S.A.S., or PdStG, as well as 100% of PDM Philippines Industries, Inc., or PPI. SMF indirectly owns the third principal French operating subsidiary, PDM Industries S.A.S., or PdM, as well as Papeteries de Malaucène S.A.S., or PdMal, and its subsidiary Malaucène Industries S.A.S., PdMal filed for liquidation during December 2011 and are no longer consolidated effective with the date of the filing. SWM HoldCo 1 owns directly 99.99% of the issued and outstanding shares of Schweitzer-Mauduit do Brasil Indústria e Comércio de Papel Ltda. (formerly known as Schweitzer-Mauduit do Brasil, S.A.), our Brazilian paper operations, or SWM-B. SWM Luxembourg owns 100% SWM RUS LLC, or SWM-RUS, a Russian company, Ipopema 94 Fundusz Inwestycyjny Zamkniêty Aktywów Niepublicznych, or Polish FIZ, a Poland company and 100% of SWM GP Luxembourg S.à.r.l, or SWM GP Lux, a Luxembourg. The Polish FIZ and SWM GP Lux own 99.9% and 0.1%, respectively, of SWM LP Luxembourg SCSP, or SWM LP Lux a Luxembourg company. SWM LP Lux owns 99.9% of SWM Poland Sp. z o.o., or SWM Poland, a Polish company and SWM Poland GP Sp z o.o. or SWM Poland GP owns the remaining 0.1%. SWM Acquisition Corp I, a holding company incorporated in Delaware directly owns 100% of DelStar, Inc., a Delaware company. DelStar, Inc. directly owns 100% of DelStar Holding Corp., a Delaware holding company which owns 100% of Coretc Tubing Corp., U.S. Netting Inc. and Delstar Technologies Inc., each Delaware companies. DelStar Technologies Inc., a company incorporated in Delaware owns 100% of two Chinese operating entities DelStar Technologies (Shanghai) Trading Corp. Ltd. and DelStar Technologies (Suzhou) Co. Ltd. We had no special purpose entities as of December 31, 2013.

Our principal executive office is located at 100 North Point Center East, Suite 600, Alpharetta, Georgia 30022-8246 and our telephone number at that address is 1-800-514-0186. Our stock is traded on the New York Stock Exchange, or NYSE, under the symbol "SWM".

AVAILABLE INFORMATION

Our Securities and Exchange Commission, or SEC, filings, which include this Annual Report on Form 10-K, Proxy Statements, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and all related amendments, are available, free of charge, on the Investor Relations section of our web site at www.swmintl.com. Information from our web site is not incorporated by reference into this Annual Report on Form 10-K. These reports are available soon after they are filed electronically with, or furnished to, the SEC. The web site allows access to historical financial information, press releases and quarterly earnings conference calls, our Code of Conduct, corporate governance guidelines, Board of Directors committee charters, as well as disclosure of any amendment to or waivers of our Code of Conduct granted to any of the principal executive officer, principal financial officer or principal accounting officer. The web site provides additional background information about us including information on our history, products and locations. Requests for information or to contact the audit committee chair, lead non-management director or to report concerns about accounting or other issues can be made in writing and sent to the Investor Relations Department at our principal executive office address listed below.

Our quarterly earnings conference calls are typically held the morning after our quarterly earnings releases and are available through our web site via a webcast. The tentative dates for our quarterly earnings conference calls related to 2014 financial results are May 7, 2014, August 6, 2014, November 5, 2014 and February 4, 2015. These dates are subject to change. Instructions on how to listen to the webcasts and updated information on times and actual dates are available through our web site at www.swmintl.com.

We have provided a Glossary of Terms at the end of this Annual Report on Form 10-K.

DESCRIPTION OF BUSINESS

Segment Financial Information. We operate and manage three reportable segments based on product lines: Paper, Reconstituted Tobacco and Filtration. The Paper segment primarily produces Cigarette Papers such as cigarette (including LIP), plug wrap and base tipping papers used to wrap various parts of a cigarette for sale to cigarette manufacturers. The Paper segment also includes commercial and industrial products such as lightweight printing and writing papers, battery separator paper, drinking straw wrap, filter paper and other specialized papers. These non-tobacco industry products are generally sold directly to converters and other end-users or brokers. The Reconstituted Tobacco segment produces reconstituted tobacco leaf, or RTL, and wrapper and binder products for sale to cigarette and cigar manufacturers. The Filtration segment produces thermoplastic nets, nonwovens, laminates, and extruded components sold to manufacturers in liquid, air and water filtration, automotive, aerospace, healthcare, industrial, food and electronics industries.

Additional information regarding "Segment Performance" is included in Part II, Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operation. In addition, selected financial data for our segments is available in Note 19, Segment Information, of the Notes to Consolidated Financial Statements. Reference is also made to Part I, Item 1A, Risk Factors, Market Risk, for a discussion regarding the risks associated with foreign operations.

Financial information about foreign and domestic operations, contained under the caption "Management's Discussion and Analysis of Financial Condition and Results of Operation" appearing in Part II, Item 7 herein and in Notes 11, 12, 15 and 19 ("Restructuring and Impairment Activities," "Debt," "Income Taxes" and "Segment Information," respectively) to the Consolidated Financial Statements contained in "Financial Statements and Supplementary Data" in Part II, Item 8 herein, is incorporated in this Item 1 by reference.

Products. We manufacture and sell paper and reconstituted tobacco products to the tobacco industry as well as specialized paper products for use in other applications. We also manufacture and sell thermoplastic nets, nonwovens, laminates, and extruded components.

Our Paper segment products include Cigarette Papers and commercial and industrial products including lightweight printing and writing papers, battery separator paper, drinking straw wrap, filter papers and other specialized papers. Each of the three principal types of Cigarette Papers - cigarette, plug wrap and base tipping papers - serves a distinct purpose in the function of a cigarette.

Cigarette paper wraps the column of tobacco in a cigarette. Certain properties of cigarette paper, such as control of ignition propensity, basis weight, porosity, opacity, tensile strength, texture and burn rate must be controlled to tight tolerances. Many of these characteristics are critical to meet the requirements of high-speed production processes utilized by cigarette manufacturers as well as their desired attributes of finished cigarettes such as reduced deliveries of tobacco-related smoke constituents. In addition to the attributes and functional requirements of conventional cigarette papers, certain of our products facilitate our customers' design of LIP cigarettes to enhance their ability to self-extinguish when they are not actively being smoked, including papers sold under our registered trademark ALGINEX® and trademark GLUCIGEN™. Our solutions pioneered this cigarette paper category.

Plug wrap paper forms the outer layer of a cigarette filter and is used to hold the filter materials in a cylindrical form. Conventional plug wrap is manufactured on flat wire paper machines using wood pulp. Porous plug wrap, a highly air-permeable paper, is manufactured on inclined-wire paper machines using a furnish consisting of long-fibers, such as abaca, and wood pulp. Porosity, a measure of air-flow permeability, ranges from a typical level of less than 100 Coresta on conventional plug wrap to 35,000 Coresta on high-porosity papers.

Base tipping paper, produced in white or tan/cork color, joins the filter element to the tobacco-filled column of the cigarette. The ability to produce tipping paper, which is both printable and glueable at high speeds, is critical to

producing a cigarette with a distinctive finished appearance.

Certain of our non-tobacco industry products use a fiber blend consisting of long-fibers. These products are generally sold directly to converters and other end-users in North America and western Europe and through brokers in Brazil.

The non-tobacco industry products are a diverse mix that includes low volume, high-value engineered papers as well as commodity paper grades produced to maximize machine utilization.

Our Reconstituted Tobacco segment products include RTL which is used as a tobacco blend with virgin tobacco in cigarettes and reconstituted tobacco wrappers and binders for cigars. These products are sold directly to tobacco companies or their designated converters in the Americas, Europe, Asia and elsewhere.

RTL is used by manufacturers of cigarettes and other tobacco products as a means of recycling their tobacco by-products and to achieve product performance attributes. We currently produce reconstituted tobacco in two forms: leaf, or RTL, in France, which is manufactured by LTRI, and wrapper and binder in the United States. RTL is used by cigarette manufacturers primarily to blend with virgin tobacco as a design aid to achieve certain attributes of finished cigarettes, such as taste characteristics and reduced deliveries of tobacco-related smoke constituents, and to cost-effectively utilize tobacco leaf waste by-products. Wrapper and binder are reconstituted tobacco products used by manufacturers of machine-made cigars. Binder is used to hold the tobacco leaves in a cylindrical shape during the production process. Wrapper is used to cover the outside of the cigar, providing a uniform, finished appearance.

Our Filtration segment products include thermoplastic nets, nonwovens, laminates, and extruded components under the trade name DELSTAR®. We manufacture plastic and metal components used in a wide range of industries and markets, including liquid, air and water filtration, automotive, aerospace, healthcare, industrial, food and electronics.

Markets and Customers. Our Paper and Reconstituted Tobacco segments supply the major, and many of the smaller, cigarette manufacturers including international tobacco companies, regional tobacco manufacturers and government monopolies.

Philip Morris International Inc., or PMI, Philip Morris-USA, a subsidiary of Altria Group Inc., Japan Tobacco Inc., or JT, and British American Tobacco, or BAT, are our four largest customers and together with their respective affiliates and designated converters, accounted for 57%, 55% and 54% of the Company's 2013, 2012 and 2011 consolidated net sales, respectively. Although the total loss of one or more of these large customers could have a material adverse effect on our results of operations, this is not considered likely given the significant share that our capacity represents of the total worldwide supply available to meet the demand for cigarette-related fine papers. A material variation in demand from one or more of these customers or due to external factors such as government legislation or changes in consumer behavior, however, could result in a significant decline in demand for our products.

The Filtration segment supplies niche products to filtration, healthcare, and industrial manufacturers. These products are highly engineered, often customized and, in some cases, we are the sole supplier of certain products to our top customers, none of which represent more than 10% of the Company's net sales.

Sales and Distribution. Essentially all tobacco-related products manufactured by both the Paper and Reconstituted Tobacco segments are sold by our marketing, sales and customer service organizations directly to cigarette manufacturers or their designated converters. Most of our Paper segment's non-tobacco related products, which represent approximately 6% to 10% of its net sales, are sold on a direct basis.

Filtration products are sold to customers by our marketing, sales and customer service organization on a direct basis.

The typical modes of transportation we utilize in the delivery of product to our customers include truck, rail and ocean-going vessels. As is typical in our industry, ownership of the product generally transfers to our customer upon shipment from our mills, except for certain export sales where ownership typically transfers at the foreign port or customer facility.

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Competition. We are the largest producer of Cigarette Papers in the world. LTRI is the leading independent producer of RTL for use in cigarettes. We do not sell our products directly to consumers or advertise our products in consumer media. The specialized nature of these tobacco-related papers requires unique research and development capability and special papermaking equipment and skills to meet exacting customer specifications. These factors have limited the number of competitors in each of the tobacco-related paper categories discussed separately below.

Paper. As the sole domestic producer of Cigarette Papers in North America, we believe that we have the majority supply position. PdM and PdStG, our indirect wholly-owned subsidiaries in France, and SWM-Poland sell most of their products in Europe. We believe SWM-B has the majority of the cigarette paper market in Brazil and in South America. Our principal competitors include delfortgroup AG, or Delfort, an Austrian corporation, Miquel y Costas & Miquel S.A., or Miquel y Costas, a Spanish corporation, Julius Glatz GmbH, an German company, and PT Bukit Muria Jaya, or BMJ, an Indonesian corporation. We believe that the bases of cigarette paper competition are price, consistent quality, security of supply, level of technical service and performance requirements of the customer's cigarette-making equipment.

We have developed, individually or in conjunction with customers, technologies to address the demand for cigarette paper for LIP cigarettes in the United States, Canada, Australia and the European Union, or EU. We believe that we are currently the leading producer of cigarette paper for LIP cigarettes and continue to actively develop the technologies for such products. We have license agreements with third parties which grant them the right to use certain of our LIP intellectual property, excluding ALGINEX® related intellectual properties.

We estimate that we hold a majority of industry share for high porosity plug wrap papers in each of the market segments in which we compete. Our competitors are Miquel y Costas and Delfort. We supply base tipping paper for North America, which is subsequently printed by converters. The principal competitors in Europe are Delfort and Julius Glatz. We estimate our Brazilian operation holds a large share for the base tipping paper market in South America, which is subsequently printed by converters. Our principal competitor in Latin America is Miquel y Costas. We believe that the bases for competition are consistent quality, price and, most importantly, the ability to meet the runability and printability requirements of converting equipment and high-speed cigarette-making machines.

We produce papers for lightweight printing and writing, battery separator papers, drinking straw wrap, filter papers and other specialized papers. We believe that price is the primary basis of competition for drinking straw wrap, printing and writing and filter papers, while consistent quality and customer service are believed to be the primary competitive factors for battery separator paper.

Reconstituted Tobacco. LTRI is the leading independent producer of RTL in the world. We believe that the basis of competition in this market is primarily quality. However, sales volumes are influenced by worldwide virgin tobacco prices and cigarette producers' various in-house tobacco reconstitution processes, as lower prices of virgin tobacco or other RTL forms may compete against reconstituted tobacco sales volumes.

LTRI's principal competitors are cigarette companies such as Philip Morris-USA, R.J. Reynolds Tobacco Company, Elets, an affiliate of Japan Tobacco Inc. which operates in Russia, and STMA (China), all of which produce RTL primarily for internal use. Huabao International Holdings Ltd, a Hong Kong company, provides tobacco reconstitution in China.

We estimate that approximately 35% of reconstituted cigar wrapper and binder used in the U.S. is produced internally by domestic cigar manufacturers. Our Reconstituted Tobacco segment's Ancram mill and Nuway Tobacco, a privately-held cast process manufacturer, produce the balance for U.S. demand which is not produced internally by domestic cigar manufacturers. The Ancram mill and DHT, a subsidiary of NV Deli Maatschappij, are the main suppliers to the European cigar manufacturers.

Filtration. Our resin-based, DelStar-branded products are leaders in their categories and compete against niche products made by Conwed, a subsidiary of Leucadia National Corp., Marshall Manufacturing Company, Johns Manville, a subsidiary of Berkshire Hathaway Inc., Hollingsworth and Vose Company, and Smith & Nephew plc. We believe our Filtration products compete primarily on product features, innovations and customer service.

Raw Materials and Energy. Wood pulp is the primary fiber used in our operations. Our operations consumed approximately 72,000 metric tons of wood pulp in both 2013 and 2012, all of which was purchased. Our operations also use other cellulose fibers, the most significant of which are in the form of flax fiber and tobacco leaf by-products, as the primary raw materials for Cigarette Papers and reconstituted tobacco products, respectively. While tobacco leaf by-products are generally the property of the cigarette manufacturer for whom the reconstitution is contracted, we purchase some tobacco leaf by-products for use in the production of RTL and wrapper and binder products.

Flax straw is purchased and subsequently processed into flax tow at our processing facility in Canada. The flax tow is then converted into flax pulp at pulping facilities in the United States and France. Flax tow and flax pulp is also purchased on the open market. Certain specialty papers are manufactured by our operations in France, requiring small amounts of other cellulose fibers, all of which are purchased.

In addition to cellulose fibers, our operations use calcium carbonate as another significant raw material in the production of many of our paper products. Calcium carbonate, or chalk, is used in the production of Cigarette Papers, as well as in certain of our other paper products, to provide desired qualities and characteristics, such as opacity, as well as end-product performance attributes. All of our needs for calcium carbonate are purchased. Our Quimperlé mill in France and Pirahy mill in Brazil have on-site, vendor-operated, precipitated calcium carbonate plants which supply significant quantities toward the needs of those mills. For the balance of their needs, our mills also purchase calcium carbonate manufactured elsewhere. Our calcium carbonate purchase commitments are discussed in Note 18, Commitments and Contingencies, of the Notes to Consolidated Financial Statements.

Manufacturing of resin-based products is highly dependent on polyethylene terephthalate, or PET, and nylon polypropylene resins. The Company has multiple sources of resin. Resin price fluctuations can impact profitability; such impacts are partially mitigated by contractual pricing adjustment mechanisms with customers.

We believe that our purchased raw materials are readily available from several sources and that the loss of a single supplier would not have a material adverse effect on our ability to procure needed raw materials from other suppliers.

The papermaking processes use significant amounts of energy, primarily electricity, natural gas and fuel oil to run the paper machines and other equipment used in the manufacture of pulp and paper. In France, Poland and in the United States, availability of energy is generally not expected to be an issue, although prices can fluctuate significantly. We enter into agreements to procure a portion of our energy requirements for future periods in order to reduce the uncertainty of future energy costs.

In France, we have entered into agreements with an energy cogeneration supplier whereby the supplier constructed and operates cogeneration facilities at our Spay and Quimperlé mills and supplies steam that is used in the operation of our mills. These cogeneration facilities provide energy cost savings and improved security of supply.

In Brazil, where production of electricity is heavily reliant upon hydroelectric plants, availability of electricity has been affected in the past by rain variations. Over the past few years the Brazilian government has taken action to improve distribution lines, which has provided a better balance of energy use throughout the country and mitigates the risk of lost energy. Our Brazilian business currently has a sufficient supply of energy to continue its current level of operation.

Additional information regarding agreements for the supply of energy is included in Note 18, Commitments and Contingencies, of the Notes to Consolidated Financial Statements.

Backlog and Seasonality. We have historically experienced a steady flow of orders. Our facilities typically receive and ship orders within a 30-day period, except for RTL where orders are generally placed well in advance of delivery. We plan our manufacturing schedules and raw material purchases based on our evaluation of customer forecasts and current market conditions.

Within the Paper segment, the U.S. operations do not calculate or maintain records of order backlogs. Its largest customer Philip Morris-USA provides forecasts of future demand, but actual orders for Cigarette Papers are typically placed two weeks in advance of shipment. In France, Cigarette Papers order backlog was approximately $37 million and $19 million on December 31, 2013 and 2012, respectively. This represented approximately 35 and 12 days of sales for the French Paper operations in 2013 and 2012, respectively. The Polish and Brazilian operation do not calculate or maintain records of order backlogs. Souza Cruz, our Brazilian operation's largest customer, provides forecasts of its future demand, typically eight weeks in advance, in order for the Brazilian operations to manage production and ensure a sufficient supply to meet this customer's anticipated requirements.

The Reconstituted Tobacco segment's RTL business operates predominantly under a number of annual supply agreements. The order backlog for RTL was approximately $99 million and $145 million on December 31, 2013 and 2012, respectively, and is typically filled within one fiscal year.

In the Filtration segment, customer orders are generally manufactured and shipped within 30 days and, in certain instances, up to three months. As of December 31, 2013, the Filtration segment order backlog was approximately $22 million.

Sales of our paper and reconstituted tobacco products are subject to significant seasonal fluctuations. In the United States and Europe, customer shutdowns of one to two weeks in duration typically occur in July and December. In Brazil, customer orders are typically lower in December due to a January and February holiday season.

Research and Development. We employ approximately 70 research and development personnel in research and laboratory facilities in Quimperlé and Spay, France, Santanésia, Brazil, Strykow, Poland, Alpharetta, Georgia, Middletown, Delaware and Austin, Texas. We are dedicated to developing product innovations and improvements to meet the needs of individual customers. The development of new components for tobacco products and the development of new non-tobacco products are the primary focuses of these research and development functions, including several development projects for our major customers. We expensed $15.3 million in 2013, $9.9 million in 2012 and $9.2 million in 2011 on research and development. We believe that our research and product development capabilities have played an important role in establishing our reputation for high quality, superior products.

Our commitment to research and development has enabled us, for example, to (i) produce high-performance papers designed to run on the high-speed manufacturing machines of our customers, (ii) produce papers to exacting specifications with very high uniformity, (iii) produce cigarette paper with extremely low basis weights, (iv) develop cigarette paper for LIP cigarettes, (v) produce highly porous cigarette and plug wrap papers, (vi) produce wrapper and binder tobacco reconstituted products, in a paper process, matching the specifications of machine-made cigars and (vii) produce papers and reconstituted tobacco products with other specifically engineered properties required for end-product performance attributes. The Filtration segment, acquired through the December 2013 purchase of DelStar, has a history of finding innovative design solutions, including products which improve the performance of customers' products and manufacturing operations. We believe that our commitment to research and development, coupled with our investment in new technology and equipment, has positioned us to take advantage of growth opportunities all around the world.

Patents and Trademarks. As of December 31, 2013, we owned 253 patents and had pending 121 patent applications covering a variety of Cigarette Papers, RTL, cigar wrapper and binder and other products and processes in the United States, western Europe and several other countries. We believe that such patents, together with our papermaking

expertise and technical sales support, have been instrumental in establishing us as the leading worldwide supplier of Cigarette Papers. We believe that patents have contributed to our position as the world's leading independent producer of papers used for LIP cigarettes. Our Filtration segment holds eight patents registered in China.

Management believes that our "ALGINEX®" water-based technology trademark and "GLUCIGEN™" trademark for use in banded papers for the production of LIP cigarettes, and the "SWM" logo and trade names have been important contributors to the marketing of our products. In our Filtration segment, "DELSTAR®," "NALTEX®", "DELNET®", "DELPORE®", "STRATEX®", and "CORETEC®" are important trade names which have high industry acceptance for marketing our products.

Administrative and Court Proceedings Relating to Papers for Lower Ignition Propensity Cigarettes. In December 2009, Miquel y Costas & Miquel S.A., Société Papéterie Leman SAS and delfortgroup AG filed Notices of Opposition to the European Patent Office's, or the EPO, grant of European Patent EP 1482815. The opponents contend that the claimed invention is not disclosed in a manner sufficiently clear and complete for it to be carried out by a person skilled in the art and that the claims were either not novel or lacked inventive step due to prior art references (including, among others, two earlier patents of SWM cited by the Examiner prior to granting the patent). The Company will continue to defend the grant of this patent by taking necessary actions including responding to further submissions by the opponents. Once the EPO considers that all positions have been fully briefed, it will hold a hearing before reaching a final conclusion on the oppositions. There is no mandated timetable by which the EPO must reach a decision. The outcome of this dispute would not prevent the Company from practicing its ALGINEX® LIP solution. The patent remains in effect and enforceable while the opposition proceedings are pending. In connection with its entrance into a worldwide LIP license agreement with SWM, delfortgroup has withdrawn its opposition and is no longer a party to these proceedings (though delfortgroup's arguments and evidence presented remain in the proceedings). The action remains open with the other parties.

On November 11, 2010, the EPO issued a Decision to Grant SWM European Patent No. 1333729. On December 8, 2010, Julius Glatz GmbH filed a Notice of Opposition to the grant of this patent. In September 2011, Papéteries du Leman, delfortgroup AG, and Miquel y Costas & Miquel S.A. each filed opposition papers and Glatz supplemented its previous filing. However, Papéteries du Leman failed to pay the opposition fee and consequently is not a party to the opposition proceedings. It subsequently refiled its opposition papers as third-party observations. The Company's response to the Notices of Opposition was timely filed. The Company believes that the EPO properly granted the patent and it intends to vigorously defend the patent. In connection with its entrance into a worldwide LIP license agreement with SWM, delfortgroup has withdrawn its opposition and is no longer a party to these proceedings (though delfortgroup's arguments and evidence presented will remain in the proceedings). The action remains open with the other parties.

A petition to reexamine United States Patent No. 6,725,867 filed by delfortgroup in 2010 is still pending. As a result of the worldwide LIP license agreement with SWM, delfortgroup has withdrawn from this proceeding. There are no other petitioners in the action.

On June 27, 2012, the EPO granted the Company's applications for two LIP-related patents, EP 2127544 and EP 2127545, that are based on divisional applications related to European Patent No. 1333729. Julius Glatz GmbH and Miquel y Costas & Miquel S.A. each filed Notices of Opposition to the grants of EP 2127544. Julius Glatz GmbH, Miquel y Costas & Miquel S.A. and Société Papéterie Leman SAS each filed Notices of Opposition to the grant of EP 2127545. The EPO issued communications requesting SWM to respond to the oppositions on May 7, 2013. The Company believes that the EPO properly granted the patents and it intends to vigorously defend the patents.

On September 12, 2012, the EPO granted the Company's LIP related patent, EP 2127543, that is based on a divisional application related to European Patent No. 1333729. Papéteries du Leman, Julius Glatz GmbH and Miquel y Costas & Miquel S.A. each filed Notices of Opposition, and the EPO issued a communication on July 23, 2013, requesting SWM to respond to the oppositions. The Company believes that the EPO properly granted the patent and it intends to vigorously defend the patent.

Employees. As of December 31, 2013, we had approximately 3,000 regular, full-time, active employees.

North American Operations. Hourly employees at the Spotswood, New Jersey, and Ancram, New York mills are represented by locals of the United Steel Workers Union. The collective bargaining agreement at our Spotswood mill is a three-year agreement which is effective through July 28, 2016. The three-year collective bargaining agreement at our Ancram mill is effective through September 30, 2014. We believe employee and union relations continue to be positive at the Spotswood and Ancram mills.

The fiber operations of our Canadian subsidiary, our Newberry, South Carolina facility and DelStar facilities are non-union. We believe that employee relations are positive.

French Operations. Hourly employees at our Quimperlé, Spay, and Saint-Girons, France mills are union represented. From time to time, we undertake certain restructuring activities in France and elsewhere and this can impact our employee relations which we believe are generally as positive as other similarly situated French manufacturing operations.

Brazilian Operations. Hourly employees at the Pirahy mill are represented by a union. The one-year collective bargaining agreement at SWM-B was renewed through May 31, 2014. We believe that employee relations are positive and comparable to other similar Brazilian manufacturing operations.

Polish Operations. Employees at our Strykow, Poland facility are non-union. We believe that employee relations in Poland are positive.

Chinese Operations. Employees at our Suzhou, China facility are non-union. We believe that employee relations in China are positive.

Environmental Matters. Capital expenditures for environmental controls to meet legal requirements and otherwise relating to the protection of the environment at our facilities in the United States, France, Brazil, Poland, China and Canada were $1.0 million in 2013 and are expected to be $1 million or less in each of the next two years, of which no material amounts were or are expected to be the result of environmental fines or settlements. These expenditures are not expected to have a material adverse effect on our financial condition, results of operations or competitive position; however, these estimates could be modified as a result of changes in our plans, changes in legal requirements or other factors.

Working Capital. We normally maintain approximately 60 to 90 days of inventories to support our operations. Our sales terms average between 15 and 60 days for payment by our customers, dependent upon the products and markets served. With respect to our accounts payable, we typically carry approximately a 30 to 60 day level, in accordance with our purchasing terms, which vary by business location. The accounts payable balance varies in relationship to changes in our manufacturing operations, particularly due to changes in prices of wood pulp, resins and purchased energy and the level and timing of capital expenditures related to projects in progress.

Executive Officers. The names and ages of our executive officers as of February 28, 2014, together with certain biographical information, are as follows:

Name	Age	Position
Frédéric P. Villoutreix	49	Chairman of the Board and Chief Executive Officer
Jeffrey A. Cook	59	Executive Vice President, Chief Financial Officer and Treasurer
Stephen Dunmead	50	Chief Operating Officer
Michel Fievez	56	Executive Vice President, Reconstituted Tobacco Business
Patrick DeLuca	48	Executive Vice President, Global Paper
Greerson McMullen	51	General Counsel and Secretary
Robert Cardin	50	Corporate Controller

There are no family relationships between any of the directors, or any of our executive officers. None of our officers were selected pursuant to any arrangement or understanding between the officer and any person other than the Company. Our executive officers serve at the discretion of the Board of Directors and are elected annually by the Board.

Frédéric P. Villoutreix was elected Chairman of the Board and Chief Executive Officer effective January 1, 2009. Mr. Villoutreix joined the Company on December 7, 2005, was elected Chief Operating Officer on February 1, 2006, and served as interim President, French Operations from December 2006 to June 2007. Mr. Villoutreix joined us in December 2005 from Compagnie de Saint-Gobain, a leading French multi-national manufacturer of engineered materials and products, where he worked since 1990. From 2001 to 2005, Mr. Villoutreix held key manufacturing positions in Europe and the United States with Saint-Gobain, including General Manager, World Construction Products and Stone, Luxembourg and Vice President, Abrasives Europe and Coated Abrasives World with 33 operating locations.

Jeffrey A. Cook was appointed Executive Vice President, Chief Financial Officer and Treasurer in February 2012. Prior to joining SWM, he served as Chief Financial Officer since 2007 of Presstek Inc., a manufacturer and distributor of products for the commercial graphics industry, including printing presses, consumables and service. Mr. Cook began his career with General Electric and served in roles of increasing financial leadership including serving as Chief Financial Officer of GE Government Services Inc. from 1990 to 1993 and Vice President Finance of the Government Services Group of Lockheed Martin Corporation. From 1996 to 1997, he was Vice President and Chief Financial Officer of Bechtel Systems and Infrastructure, a division of Bechtel Group Inc. He was Vice President Finance of Moore North American, a division of Moore Corporation from 1997 to 2000. Mr. Cook served as Senior Vice President, Chief Financial Officer and Chief Information Officer of Kodak Polychrome Graphics, a joint venture between Eastman Kodak and Sun Chemical from 2000 to 2005.

Stephen Dunmead has served as Chief Operating Officer since March 2013. Previously, Mr. Dunmead served as the Executive Vice President and General Manager of OM Group's Specialties Division. OM Group, Inc. is a leading global solutions provider of specialty chemicals, advanced materials and unique technologies. Mr. Dunmead joined OM Group in 1998 as Director of Research and Development, Powdered Metals Division, was appointed Chief Technology Officer in 2001, and during his 14-year tenure with the organization rose through the ranks to the Executive Vice President and General Manager position.

Michel Fievez was appointed Executive Vice President, Reconstituted Tobacco Business during March 2010. He held the position of President - European Operations from June 2007 to March 2010. From 2003 to May 2007, Mr. Fievez served as General Manager One Side Coated Papers and then Vice President and General Manager Packaging, Metalizing and Office and Graphic with Ahlstrom Corporation. From 1998 to 2003, he held key manufacturing positions, including Managing Director, with Chesapeake Display and Packaging in Europe, and from 1994 to 1998, held the position of Vice President Manufacturing and Technology with Mead Packaging Europe.

Patrick DeLuca has served as Executive Vice President, Global Paper since June 2013. Previously, he was Vice President and General Manager of the Advanced Materials Business at OM Group, Inc. Mr. DeLuca joined OM Group in 1998 as a Project Manager and was promoted repeatedly to roles of increasing scope and responsibility including Plant Manager, Director of Research and Development, Director of Corporate Engineering, Purchasing and Logistics, and Business Director for the Inorganics Business.

Greerson McMullen has served as served as General Counsel & Secretary since May 2013. Previously, Mr. McMullen served as the Senior Vice President, General Counsel, Government Affairs & Secretary of the ServiceMaster Company since November 2007 (holding the Government Affairs title since March 2010). The ServiceMaster Company is a residential services company.

Robert Cardin has served as our Corporate Controller since November 2013. Previously, Mr. Cardin served as Controller for Syncreon, a specialized provider of integrated logistics services to global industries, since 2011. Prior to that time he was employed by DENTSPLY International Inc., a worldwide manufacturer of dental products, as Assistant Corporate Controller from 2010 to 2011 and as Group Controller - Dental Consumables Business from 2004 to 2010.

Item 1A. Risk Factors

Factors That May Affect Future Results

Many risk factors both within and outside of our control could have an adverse impact on our business, financial condition, results of operations and cash flows and on the market price of our common stock. While not an exhaustive list, the following important risk factors could affect our future results, including our actual results for 2014 and thereafter and could also cause our actual results to differ materially from those expressed in any forward-looking statements we have made or may make.

We expect our business to be impacted by governmental actions relating to tobacco products, as well as decreased demand for tobacco products relating to declining social acceptance of smoking in the United States and certain other countries.

In 2013, approximately 93% of our net sales were from products used by the tobacco industry in making cigarettes or other tobacco products. In recent years, governmental entities around the world, particularly in the United States, Brazil, Australia and western Europe, have taken, or have proposed, actions that had, and are likely to continue to have, the effect of reducing consumption of tobacco products which can, in turn, reduce demand for our products. Reports with respect to the possible harmful physical effects of cigarette smoking, including second-hand smoke, and use of other tobacco products have been publicized for many years. Such reports, together with actions to regulate, restrict or prohibit the sale, advertisement and promotion of tobacco products, including cigarettes and their components, to limit smoking in public places, to control or restrict additives that may be used in tobacco products and to increase taxes on such products, are intended to discourage the consumption of traditional cigarettes and other such products. In recent years, certain governmental entities, particularly in North America and Europe, have enacted, considered or proposed actions that would require cigarettes to meet specifications aimed at reducing their likelihood of igniting fires when the cigarettes are not actively being smoked. It is not possible to predict the additional legislation or regulations relating to tobacco products that may be enacted or the extent to which such legislation, regulations or the development of new products or technologies, such as e-cigarettes, may impact the design or formulation of our customers' products, the demand for traditional cigarettes and our business and financial performance.

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Cigarette consumption in the United States and western Europe has declined, in part due to the actions described above, to the diminishing social acceptance of smoking and to private actions to restrict smoking. These declines have had an adverse effect on demand for our products in these regions and potentially other regions. We expect such factors will continue to reduce smoking levels and potentially adversely affect demand for our products. In addition, litigation is pending against major manufacturers of consumer tobacco products seeking damages for health problems allegedly resulting from the use of tobacco in various forms. It is not possible to predict the outcome of such litigation or the effect adverse developments in pending or future litigation may have on the tobacco industry or its demand for our products, but in the past, increases in taxes and litigation have adversely affected demand. In the U.S., the regulatory jurisdiction of the federal Food and Drug Administration was extended in 2009 to include tobacco products, which products are now subject to product component disclosure regulations, new controls on ingredients, and additional restrictions relating to marketing and labeling. The federal Food and Drug Administration could promulgate additional regulations to areas it has not to date regulated or has only lightly regulated such as certain cigars. In Brazil, regulations limit the use of additives to cigarettes. In the European Union, the Tobacco Products Directive regulates the content, effects, marketing and labeling of tobacco products, and both revisions to the Directive and the ongoing phase-in of the REACH regulation (Registration, Evaluation, Authorization, and Restriction of Chemical Substances) may further restrict product ingredients. Additionally, the World Health Organization is actively promoting tobacco regulation, and other countries worldwide are in the process of adopting some or all of these restrictions. The impact of these legislative and regulatory initiatives on the production and sale of our and our customers' products is not presently known but could adversely affect our results.

The overall demand in the U.S. and western Europe for conventional tobacco cigarettes has generally been declining in terms of volume of sales. In addition to the governmental actions referred to above, there is and continues to be a decline in the social acceptability of smoking and increased awareness of health risks relating to tobacco products. Such a decline could lead to certain merchants deciding not to sell tobacco products, thus potentially adversely impacting demand for our products.

Our technological advantages are unlikely to continue indefinitely.

We consider our intellectual property and patents to be a material asset. We have been at the forefront of developing new products and technology within our industries and have patented several of our innovations, particularly with regard to cigarette paper used to produce LIP cigarettes. This has enhanced our ability to sell products and to provide added function and other value to the products we sell allowing them to command higher margins. This advantage has also enabled us to license certain of our patents and know-how and earn royalty income from competitors and customers. Presently, we are seeing evidence of increasing efforts and activity by our competitors and some customers to develop and sell competitive products, particularly in the area of papers used for lower ignition propensity applications and e-cigarettes. Over time, we expect our competitors to develop competitive products that are designed to avoid our intellectual property or to license our innovations. Ultimately, our patents will expire. As we expand our production of LIP papers, RTL and our Filtration operations to more locations and countries, the risk of the loss of proprietary trade secrets will increase, and any significant loss would result in the loss of the competitive advantages provided by such trade secrets. While we cannot predict the impact or the timing of these trends and eventualities, they likely will reduce our sales and margins from the levels that we otherwise would have achieved.

Effectively policing our domestic and international intellectual property and patent rights is costly and may not be successful.

Our portfolio of granted patents varies by country, which could have an impact on any competitive advantage provided by patents in individual markets. We rely on patent, trademark, and other intellectual property laws of the United States and other countries to protect our intellectual property rights. In order to maintain the benefits of our patents, we may be required to enforce certain of our patents against infringement through judicial or administrative actions. However, we may be unable, or it may be uneconomic for us, to prevent third parties from using our

intellectual property or infringing on our patents without our authorization, which may reduce any competitive advantage we have developed. If we have to litigate to protect these rights, any proceedings could be costly, time consuming, could divert management resources, and we may not prevail. We cannot guarantee that any United States or foreign patents, issued or pending, will continue to provide us with any competitive advantage or will not be successfully challenged by third parties.

We do not believe that any of our products infringe the valid intellectual property rights of third parties. However, we may be unaware of intellectual property rights of others that may cover some of our products or services or a court or other governmental body may come to a different conclusion from ours. In that event, we may be subject to significant claims for damages or disruptions to our operations. Effectively policing our intellectual property and patents is time-consuming and costly, and the steps taken by us may not prevent infringement of our intellectual property, patents or other proprietary rights in our products, technology and trademarks, particularly in foreign countries where in many instances the local laws or legal systems do not offer the same level of protection as in the United States.

In December 2009, Miquel y Costas & Miquel S.A., delfortgroup AG, and Société Papéterie Leman SAS filed Notices of Opposition to the European Patent Office's, or EPO, grant of European Patent EP 1482815. The opponents contend that the claimed invention is not disclosed in a manner sufficiently clear and complete for it to be carried out by a person skilled in the art and that the claims were either not novel or lacked inventive step due to prior art references, amongst others, two earlier patents of SWM, cited by the Examiner in granting the patent. The Company will continue to defend the grant of this patent by taking necessary actions including responding to further submissions by the opponents. Once the EPO considers that all positions have been fully briefed, it will hold a hearing to assist it in reaching a final conclusion on the oppositions. There is no mandated timetable by which the EPO must reach a decision. The outcome of this dispute would not prevent the Company from practicing its ALGINEX® LIP solution. The patent remains in effect and is enforceable while the opposition proceedings are pending. As a result of the world-wide LIP license agreement with SWM, delfortgroup has withdrawn its opposition and is no longer a party to these proceedings; although, delfortgroup's arguments and evidence presented remain in the proceedings. The action remains open with the other parties.

On November 11, 2010, the EPO issued a Decision to Grant SWM European Patent No. 1333729. On December 8, 2010, Julius Glatz GmbH filed a Notice of Opposition to the grant of this patent. In September 2011, Papéteries du Leman, Miquel y Costas & Miquel S.A. and delfortgroup AG each filed opposition papers and Glatz supplemented its previous filing. Papéteries du Leman failed to pay the opposition fee and thus is not a party to the opposition proceedings; however, it refiled its opposition papers as third-party observations. The Company believes that the EPO properly granted the patent and it intends to vigorously defend the patent. The patent remains in effect and is enforceable while the opposition proceedings are pending. As a result of the world-wide LIP license agreement with SWM, delfortgroup has withdrawn its opposition and is no longer a party to these proceedings; although, delfortgroup's arguments and evidence presented will remain in the proceedings. The action remains open with the other parties.

On June 27, 2012, the EPO granted the Company's applications for two LIP-related patents, EP 2127544 and EP 2127545, that are based on divisional applications related to European Patent No. 1333729. Julius Glatz GmbH and Miquel y Costas & Miquel S.A. each filed Notices of Opposition to the grants of EP 2127544. Julius Glatz GmbH, Miquel y Costas & Miquel S.A and Société Papéterie Leman SAS each filed Notices of Opposition to the grant of EP 2127545. The EPO issued communications requesting SWM to respond to the oppositions on May 7, 2013. The Company believes that the EPO properly granted the patents, and it intends to vigorously defend the patents. The patent remains in effect and is enforceable while the opposition proceedings are pending.

On September 12, 2012, the EPO granted the Company's LIP-related patent, EP 2127543, that is based on a divisional application related to EP 1333729. Papéteries du Leman, Julius Glatz GmbH and Miquel y Costas & Miquel S.A. each filed Notices of Opposition, and the EPO issued a communication on July 23, 2013, requesting SWM to respond to the oppositions. The Company believes that the EPO properly granted the patent, and it intends to vigorously defend the patent. The patent remains in effect and is enforceable while the opposition proceedings are pending.

Our financial performance can be significantly impacted by the cost of raw materials and energy.

Raw materials are a significant component of the cost of the products that we manufacture. The cost of wood pulp, which is the largest component of the raw materials that we use, and of resins by our Filtration segment are highly cyclical and can be more volatile than general consumer or producer inflationary changes in the general economy. For instance, during the period from January 2011 through September 2013, the U.S. list price of northern bleached softwood kraft pulp, or NBSK, a representative pulp grade that we use, ranged from a low of $830 per metric ton in September 2012 to a high of $1,035 per metric ton in June 2011. Also, over the last five years, the cost of polypropylene has fluctuated from 35 cents per pound to 105 cents per pound. We periodically enter into agreements with customers under which we agree to supply products at fixed prices. As a consequence, unanticipated increases in the costs of raw materials, or the lack of availability of such raw materials (due to force majeure or other reasons), can significantly impact our financial performance. Even where we do not have fixed-price agreements, we generally cannot pass through increases in raw material costs in a timely manner and in many instances are not able to pass through the entire increase to our customers.

Paper manufacturing is energy-intensive. In France, Poland and in the United States, availability of energy generally is reliable, although prices can fluctuate significantly based on variations in overall demand. Western Europe is becoming significantly dependent on energy supplies from the Commonwealth of Independent States, which in the past has demonstrated a willingness to restrict or cut off supplies of energy to certain customers. The volume of oil or gas flowing through pipeline systems that ultimately connect to western Europe also has been cut off or restricted in the past, and such actions have the capability of adversely impacting the supply of energy to western Europe and, consequently, the cost and availability of electricity to our European operations. In Brazil, where production of electricity is heavily reliant upon hydroelectric plants, availability of electricity can be, and has in the past been, affected by rain variations. Although our Brazilian business currently has a sufficient supply of energy to continue its current level of operation, there can be no assurance that we will have sufficient supply in the future. Due to the competitive pricing for most of our products, we typically are unable to fully pass through higher energy costs to our customers. Periodically, when we believe it is advantageous to do so, we enter into agreements to procure a portion of our energy for future periods in order to reduce the uncertainty of future energy costs. However, in recent years this has only marginally slowed the increase in energy costs due to the volatile changes in energy prices we have experienced.

Historically, we have experienced significant cost savings and productivity benefits relating to our ongoing Operational Excellence program; however, these benefits may not continue indefinitely.

Historically, we have experienced significant cost savings and productivity benefits relating to our ongoing Operational Excellence program that have supported our margins during periods of significant attrition in the Tobacco industry. We expect to continue to achieve significant savings and benefits from this program, however, in light of continued industry attrition, execution risks and other factors, should we be unable to continue to obtain these savings and benefits in line with historical achievements, our profitability and financial results could be adversely affected.

Because of the geographic diversity of our business, we are subject to a range of international risks.

We have manufacturing facilities in six countries, two joint ventures in China and sell products in over 90 countries, many of which are emerging and undeveloped markets. Our manufacturing operations, sales and results, depending on their location, are subject to various international business risks, including the following:

- Foreign countries can impose significant import, export, excise and income tax and other regulatory restrictions on business, including limitations on repatriation of profits and proceeds of liquidated assets. While we attempt to manage our operations and international movements of cash from and amongst our foreign subsidiaries in a tax-efficient manner, unanticipated international movement of funds due to unexpected changes in our business or changes in tax and associated regulatory schemes could result in a material adverse impact on our financial condition or results of operations;

- We are exposed to global as well as regional macroeconomic and microeconomic factors, which can affect demand and pricing for our products, including: unsettled political and economic conditions; expropriation; import and export tariffs; regulatory controls and restrictions; and inflationary and deflationary economies. These factors together with risks inherent in international operations, including risks associated with with any non-compliance with the U.S. Foreign Corrupt Practices Act, the 2013 Brazilian Clean Companies Act, the U.K. Bribery Act 2010, the 2013 Russian Law on Preventing Corruption and other non-U.S. anti-bribery law compliance, could adversely affect our results;

- We participate in two joint ventures and have one manufacturing facility in China. One joint venture sells our products primarily to Chinese tobacco companies. The second joint venture is building a new reconstituted tobacco mill in China. Operations in China entail a number of risks including international and domestic political risks, the need to obtain operating and other permits from the government, changes in the policies or in our relations with government-owned or run customers and to operate within an evolving legal and economic system; and

- Changes in international trade sanctions may restrict or prohibit us from transacting business with established customers. Since December 2012, we have held a license from the U.S. Office of Foreign Assets Control to continue selling reconstituted tobacco for distribution in Iran. Our continued sales of reconstituted tobacco in Iran are contingent on our successfully obtaining annual renewals of this license.

Changes in the laws and regulations described above, adverse interpretations or applications of such laws and regulations, and the outcome of various court and regulatory proceedings in Europe and Brazil could adversely impact the Company's business in a variety of ways, including increasing expenses, decreasing sales, limiting its ability to repatriate funds and generally limiting its ability to conduct business, all of which could adversely affect our operations and financial results.

Fluctuations in foreign currency exchange rates could adversely impact our financial condition and results of operations.
A significant portion of our revenues are generated from operations outside the United States. In addition, we maintain significant operations and acquire or manufacture many of our products outside the United States. The functional currency of our international subsidiaries is generally the local currency in which each subsidiary operates. In particular, a large portion of our commercial business is denominated in euros. Our consolidated financial statements are presented in U.S. dollars. Therefore, we must translate revenues, expenses, assets and liabilities from functional currencies into U.S. dollars at exchange rates in effect during, or at the end of the reporting period. As a result, our future revenues, costs and results of operations could be significantly affected by changes in foreign currency exchange rates, especially the euro to U.S. dollar exchange rate.

In addition, some of our sale and purchase transactions are denominated in a currency other than the local currency of our operations. As a result, changes in exchange rates between the currencies in which the transaction is denominated versus the local currency of our operation into which the transaction is being recorded can impact the amount of local currency recorded for such transaction. This can result in more or less local currency revenue or cost related to such transaction and thus have an effect on our operating profit. Currency transaction risk is mitigated partially in France because some of the revenue and expense transactions of our French subsidiaries are denominated in U.S. dollars, providing a degree of natural hedging. Our Brazilian and Polish operations are more fully exposed to currency transaction risk, especially as a result of U.S. dollar and euro denominated sales, respectively.
Changes in foreign currency exchange rates also impact the amount reported in other income (expense), net. For instance, when a non-local currency receivable or payable is not settled in the period in which it is incurred, we are required to record a gain or loss, as applicable, to reflect the impact of any change in the exchange rate as of the end of the period. We also have to reflect the translation rate impact on the carrying value of our foreign assets and liabilities as of the end of each period, which is recorded as Unrealized Translation Adjustment in Other Comprehensive Income.

We utilize a variety of practices to manage this risk, including operating and financing activities and, where considered appropriate, derivative instruments. All derivative instruments we use are either exchange traded or entered into with major financial institutions in order to reduce credit risk and risk of nonperformance by third parties. Counterparty risk cannot be eliminated and there can be no assurance that our efforts will be successful. We generally hedge foreign currency transactions risk primarily through the use of derivative instruments, including forward and swap contracts and, to a lesser extent, option contracts. The use of derivative instruments is intended to mitigate or reduce transactional level volatility in the results of foreign operations, but does not completely eliminate volatility. If our future revenues, costs and results of operations are significantly affected by economic conditions abroad and we are unable to effectively hedge these risks, they could materially adversely affect our results of operations and financial condition.

We are dependent upon the availability of credit, and changes in interest rates can impact our business.

We supplement operating cash flow with bank borrowings under a credit agreement with a syndicate of banks that matures in December 2018. To date, we have been able to access credit when needed and on commercially reasonable terms. However, deterioration of credit markets, including an economic crisis in the U.S. or elsewhere, whether or not caused by the U.S. or European debt ceiling, deficits and budget issues could have an adverse impact on our ability to negotiate new credit facilities or access or renew our existing one. Constraints on the availability of credit, or the unavailability of credit at reasonable interest rates, would negatively impact our business, including potentially impairing our ability to declare dividends, conduct share buy-backs and make acquisitions.

Our credit facility contains financial covenants that we have historically fulfilled, and we do not presently anticipate any events that would impair our ability to meet those covenants in the future. However, in the event of material unforeseen events that impact on our financial performance, particularly during a time when we have material amounts of debt, a situation could arise where we are unable to fully draw from our existing credit facility notwithstanding that there is otherwise available capacity.

We have a combination of variable and fixed-rate debt consisting of short-term and long-term instruments. We selectively hedge our exposure to interest rate increases on our variable rate long-term debt when we believe that it is practical to do so. We have utilized various forms of interest rate hedge agreements, including interest rate swap agreements and forward rate agreements. There can be no certainty that our hedging activities will be successful or fully protect us from interest rate exposure.

Seasonality can impact our business.

Sales of our Paper and Reconstituted Tobacco products in the United States, Europe and Brazil are subject to seasonal fluctuations. In the United States and Europe, customer shutdowns typically occur in July and December and historically have resulted in reduced net sales and operating profit during those two months. Additionally, our facilities occasionally shut down equipment to perform additional maintenance during these months or as a result of slow demand, resulting in higher product costs, higher maintenance expenses and reduced operating profit. In Brazil, customer orders are typically lower in December due to a holiday season during much of January and February.

We face competition from several established competitors and have limited market transparency.

Our four largest competitors are delfortgroup AG (Delfort), Julius Glatz GmbH (Glatz), Miquel y Costas & Miquel S.A. and PT BUKIT Muria Jaya (BMJ). All four primarily operate from modern and cost-effective mills in western Europe and Asia and are capable and long-standing suppliers to the tobacco industry. Further, three such competitors, Delfort, Glatz and BMJ, are privately held and the third, Miquel y Costas, is a closely held public company. Thus, their financial results and other business developments and strategies are not disclosed to the same extent as ours, which provides them some advantage in dealing with customers. Given the concentration of most of our competitors in western Europe, which has declining demand and has labor laws that make reducing capacity expensive and slow, excess capacity exists and therefore price competition is acute. We believe that all four competitors have good relationships with the multinational cigarette companies, as does the Company. The multinational cigarette companies have been known to use these close relationships to encourage the development of enhanced competition through supporting competitive products and facilities, especially when confronted with new, high-value technologies such as porous plug wrap in the past and LIP today.

As a result of the foregoing, the Company faces significant selling price, sales volume and new product risks from its competitors, especially during periods in which the Company's contracts with its major customers are subject to renewal or renegotiation.

Currently, fine papers used to produce cigarettes are only exported on a limited basis from available capacity in China and other Asian locations to western multinational cigarette companies due to government taxes and tariffs, which limit price competitiveness, as well as due to customer preferences. Should conditions change in this regard, capacity that currently is operating in China and elsewhere in Asia would present a risk to our competitive position in the developed world and elsewhere and place further pressure on our legacy paper production platforms.

Due to many of the factors described above, we have a limited ability to predict trends in the industry and there may be a time lag before we become aware of developing trends in the industry. In the RTL market segment, demand is a function, among other things, of smoke delivery regulations, the cigarette manufacturer's desire for a uniform and consistent product, the taste profile sought by cigarette manufacturers and the cost of recycling the tobacco by-product scraps relative to the cost of virgin tobacco products. Thus, our RTL business is also subject to competitive risk from lower cost virgin tobacco leaf or other, cheaper, cigarette fillers. These factors could result in lower volumes for our RTL business, resulting in downtime of certain production machines and, in some cases, accelerated depreciation or impairment charges for certain equipment as well as employee severance expenses associated with downsizing or restructuring activities.

Further, as a result of excess capacity in the tobacco-related papers industry and increased operating costs, competitive levels of selling prices for certain of the Company's products are not sufficient to cover those costs with a margin that the Company considers reasonable. Such competitive pressures have resulted, and could result in the future, in downtime of certain production machines and, in some cases, accelerated depreciation or impairment charges for certain equipment as well as employee severance expenses associated with downsizing or restructuring activities.

We are dependent upon a small number of customers for a significant portion of our sales. The loss of one or more of these customers could have a material adverse effect on our business.

Four customers accounted for over 57% of our net sales in 2013. The loss of one or more of these customers, or a significant reduction in their purchases, particularly those that impact our value-added LIP papers or reconstituted tobacco, could have a material adverse effect on our results of operations and financial results. The enhanced capabilities provided by RTL in the area of product design and regulatory compliance are important to our customers. However, future RTL results could be adversely affected by fluctuations in customer inventories, changes in the cigarette tobacco blending approaches by our customers, changes in regulations and tariffs and the price of virgin tobacco leaf.

In addition, significant consolidation has occurred among our customers, thereby increasing our dependence upon a fewer number of customers and increasing the negotiating leverage of the customers that survive. If any of our customers were to change suppliers, in-source production of reconstituted tobacco or cigarette papers (including those used to produce LIP cigarettes), institute significant cost-cutting measures or experience financial difficulty, then these customers may substantially reduce their purchases from us, which could adversely impact our operations and financial results. In addition, adverse results in the negotiation of any of our significant customer contracts, the terms of which are typically negotiated every one to three years, could significantly impact our operations and financial results.

Our business is subject to various environmental risks.

Our facilities are subject to significant federal, state, local and foreign environmental protection laws with respect to air, water and other emissions as well as the disposal of solid waste. We believe we are operating in substantial compliance with these laws and regularly incur capital and operating expenditures in order to maintain future compliance. However, these laws may change, which could require changes in our practices, additional capital expenditures or loss of carbon credits, and we may discover aspects of our business that are not in compliance. Violation of these laws can result in the imposition of significant fines and remediation costs. In France, we presently have sufficient authorized capacity for our emissions of carbon dioxide. However, this authorization must be renewed every five years. We cannot predict that we will have sufficient authorized capacity to conduct our operations in France as presently conducted or to do so without having to make substantial capital expenditures in future years. There also is the possibility of regulation of carbon dioxide emissions in the U.S. It is not presently possible to assess what, if any, impact such regulations might have on our domestic U.S. operations.

We are a member of a potentially responsible party group (Global PRP Group) that has entered into a settlement with the State of New Jersey concerning the remediation of a landfill site in Middlesex County, New Jersey. The landfill remediation has been completed. We have established a reserve of less than $0.1 million that we believe is adequate to cover our ongoing liability, but we remain exposed to post-closure operating costs over an extended period of years that cannot be fully known or estimated at this time.

Although we are not aware of any environmental conditions at any of our facilities that could have a material adverse effect on our financial results, we own facilities in France, the U.S. and elsewhere that have been operated over the course of many decades. We may face higher disposal and clean-up costs to replace equipment or facilities containing materials that were compliant when installed, but are now considered contaminants. Additionally, as we sell closed facilities, we may be required to perform additional environmental evaluations that could identify items that might require remediation or other action, the nature, extent and cost of which are not presently known.

We are subject to various legal actions and other claims.

We regularly are involved in legal actions and other claims arising in the ordinary course of business and otherwise. We are also subject to many laws and regulations around the world. Despite our efforts, we cannot guarantee that we are in compliance with every such law or regulation. Because of the complexity of Brazilian tax laws and court systems, legal actions are a particular risk affecting our Brazilian operations. Although we believe that our positions in pending disputes about state and federal taxes are correct and will ultimately be upheld by Brazilian courts, the outcome of legal proceedings can be difficult to predict. An adverse result in one or more of these tax disputes could have a material adverse impact on our financial condition and results or operations. We are also subject a various other litigation in Brazil, including labor and workplace safety claims. Although we do not believe that any of the currently pending actions or claims against us will have a material adverse impact on our business or financial condition, we cannot provide any assurances in this regard. Information concerning some of these actions that currently are pending is contained in Note 18, Commitments and Contingencies, of the Notes to Consolidated Financial Statements and in Part I, Item 3, “Legal Proceedings” of this report.

Our internal and external expansion plans and asset dispositions entail different and additional risks relative to the rest of our business.

We may from time to time consider acquisitions either within the tobacco industry or outside the industry in connection with our diversification initiatives, such as our recent acquisition of DelStar, Inc. This could involve confidential negotiations that are not publicly announced unless and until those negotiations result in a definitive agreement. Although we seek to maintain or improve the economic fundamentals of our business, it is possible that an acquisition could adversely impact our results, credit ratings or the outlook of our business. Also, acquisition opportunities are limited and present risks of failing to achieve strategic objectives or anticipated synergies or returns. There can be no assurance that we will be able to acquire attractive businesses on favorable terms, that we will realize the anticipated benefits or profits through acquisitions or that acquisitions will be accretive to earnings. Changes in our portfolio of businesses, assets and products, whether through acquisition, disposition or internal growth, present additional risks. Such activities, including diversification and our acquisition of DelStar, can lead us to incur unknown or new types of liabilities, subject us to new regulatory frameworks, new market risks, involve operations in new geographies with challenging labor, regulatory and tax regimes as well as the execution risks associated with such activities. The potential future expansion of our filtration operations could cause these operations, including DelStar, to face additional competition from larger and more established competitors than is currently the case.

The ability to dispose of idled assets and the value that may be obtained relative to their book value can result in significant impairment charges. Some of these risks manifested themselves in early 2011 when we announced suspension of construction of a wholly-owned reconstituted tobacco mill in the Philippines and could be encountered in other forms to the extent that we construct a new reconstituted tobacco mill in China through a 50% joint venture. Building a new mill or other facility is a major construction project and entails a number of risks, including the possibility that the contractors and sub-contractors who are expected to build the facility and supply the necessary equipment do not perform as expected, that there will be cost overruns or that design defects or omissions cause the facility to perform at less than projected efficiency or at less than projected capacity. In addition, commencement of production at a new site is time consuming and requires customer testing and acceptance by customers, and potentially by regulators, of the products that are produced. Also, while we anticipate sufficient demand for the site's output, there can be no assurances that the expected demand will materialize. For more information on our expansion plans, see Part II, Item 7. "Management's Discussion and Analysis of Financial Condition and Results of Operation" of this report.

We also expect to continue to expend resources to diversify and expand our product portfolio. Research and development and product diversification have several inherent risks, including technical success, market acceptance, new regulations and potential liabilities. We cannot guarantee that such efforts will succeed or that we will achieve a

satisfactory return on such expenditures.

We may not successfully integrate acquisitions and may be unable to achieve anticipated cost savings or other synergies.

The integration of acquired companies' operations involves a number of risks and presents financial, managerial and operational challenges. We may have difficulty, and may incur unanticipated expenses related to, integrating information systems, financial reporting activities, and integrating and retaining management and personnel from acquired companies. Additionally with respect to our DelStar Acquisition, we may not be able to achieve anticipated cost savings or commercial or growth synergies, for a number of reasons, including contractual constraints and obligations or an inability to take advantage of expected commercial opportunities, increased operating efficiencies or commercial expansion of key technologies. Failure to successfully integrate acquired companies may have an adverse effect on our business, results of operations, financial condition and cash flow.

Restructuring activities significantly impact our business.

We began significant restructuring activities in 2006 and 2007 in France and the United States, during 2007 in Brazil and during 2012 in the Philippines that have become part of an overall effort to improve an imbalance between demand for our products and our paper production capacity as well as improve our profitability and the quality of our products. We expect to continue these restructuring efforts from time to time. Restructuring of our existing operations, or as a results of acquisitions, involves issues that are complex, time-consuming and expensive and could significantly disrupt our business. The challenges involved in executing the actions that are part of our ongoing and, potentially future, restructuring plans include:

- demonstrating to customers that the restructuring activities will not result in adverse changes in service standards or business focus;
- consolidating administrative infrastructure and manufacturing operations while maintaining adequate controls throughout the execution of the restructuring;
- preserving distribution, sales and other important relationships and resolving potential conflicts that may arise;
- minimizing the diversion of management attention from ongoing business activities;
- maintaining employee morale, retaining key employees, maintaining reasonable collective bargaining agreements and avoiding strikes, work stoppages or other forms of labor unrest while implementing restructuring programs that often include reductions in the workforce;
- securing government approval of such plans, where necessary, and managing the litigation and associated liabilities that often are associated with restructuring actions;
- coordinating and combining operations, which may be subject to additional constraints imposed by collective bargaining agreements and local laws and regulations; and
- achieving the anticipated levels of net cost savings and efficiency as a result of the restructuring activities.

If we do not achieve expected benefits as a result of our legal entity realignment, the ability to achieve our financial guidance for operating results and cash-flow could be adversely affected.

We are re-examining our legal entity structure and certain internal business operations in order to allow us to improve our cash-flows, have easier access to our foreign cash, centralize certain internal business activities and reduce our overall effective tax rate. Initial steps to accomplish these objectives have been taken and are continuing. A significant portion of these activities is expected to be completed around the middle of 2014. However, we anticipate that there could be further activities in these respects after that.

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Realignments present significant potential risks of events occurring that could delay, halt or adversely affect the success of the project, including delays encountered in finalizing the scope of, and implementing, the realignment, the failure to achieve targeted benefits or savings, the failure to follow appropriate regulatory requirements or internal processes and procedures and a potential decrease in employee morale. Further, despite obtaining certain tax rulings, there can be no assurance that the taxing authorities of the jurisdictions in which we operate, or to which we are otherwise deemed to have sufficient tax nexus, will not challenge the tax benefits that we expect to realize as a result of the realignment. In addition, changes to U.S. or non-U.S. tax laws may negatively impact the anticipated benefits of the proposed realignment. Any future benefits to our effective tax rate will also depend on our ability to operate our business in a manner consistent with the regulatory requirements for such a realignment including applicable taxing provisions, as well as us realizing our anticipated profits. Further, we expect to incur certain costs in connection with the realignment and we may incur additional cost that are not currently expected to be incurred.
To the extent these risks or circumstances occur, we may fail to achieve the future financial and business benefits that we anticipate as a result of the realignment and our future operating results, financial condition and cash-flows may be negatively impacted. Thus, there can also be no assurance that we will realize the expected future benefits of the restructuring.
One portion of our business is dependent upon a single mill; We have limited cross redundancy across our facilities.

Sales of reconstituted tobacco leaf products represent a substantial portion of our revenues and profits. We presently produce reconstituted tobacco leaf at only one facility located in France and wrapper and binder products at only one facility located in Ancram, New York. The loss of or the interruption of operations for a significant length of time due to a casualty event or otherwise at either facility could have a material adverse effect on our business. Further, in order to achieve operational efficiencies, among other reasons, we have limited ability to shift production across our various facilities, thus the loss of production at one facility may not be able to be mitigated by increased production at another.

Significant impairment charges could result from our evaluation of the Philippines RTL manufacturing site.

The Company suspended construction of its Philippines RTL manufacturing site during 2011. The carrying value of the partially constructed assets is evaluated for impairment at each reporting period by assessing the recoverability of the costs based on the undiscounted cash flows of the operation, the likelihood of its reactivation and any alternative uses for the equipment. This evaluation, along with potential declines in our RTL volumes, resulted in 2013 in an impairment of $37.2 million and could result in a decision to record a further impairment of some or a substantial portion of the net book value of the RTL Philippines property, plant and equipment, which was $31.5 million as of December 31, 2013.

A failure of a key information technology system or process or other unusual events could adversely affect our business.

We rely extensively on information technology systems, some of which are managed by third-party service providers, to analyze, process and manage transactions and data. We also rely heavily on the integrity of this data in managing our business. We or our service providers could experience errors, interruptions, delays or cessations of service in key portions of our information technology infrastructure, which could significantly disrupt our operations and be expensive time-consuming and resource-intensive to remedy.

Natural disasters, pandemics and other unusual events could interrupt one or more of our facilities in six different countries to varying degrees, which could adversely affect our results.

We rely on a limited number of key employees and may experience difficulty in retaining, attracting and hiring qualified new personnel in some areas of our business.

The loss of any of our key employees could adversely affect our business. Because our core products relate to the tobacco industry, we may experience difficulty in retaining and hiring qualified executives and other personnel. This may be caused by the health and social issues associated with the tobacco industry. The tobacco industry competes for talent with consumer products and other companies that enjoy greater acceptance. The loss of services of any key employees, including in our DelStar business, or our inability to attract, hire and retain personnel with requisite skills could restrict our ability to develop new products, enhance existing products in a timely manner, sell products or manage our business effectively. These factors could have a material adverse effect on our business, results of operations and financial condition.

Our business depends upon good relations with our employees.

We employ approximately 3,000 employees, including manufacturing employees represented by unions. Although we believe that employee and union relations are generally positive, there is no assurance that this will continue in the future. We may experience difficulties in maintaining appropriate relations with unions and employees in certain locations. Problems or changes affecting employees in certain locations may affect relations with our employees at other locations. The risk of labor disputes, work stoppages or other disruptions in production could adversely affect us especially in conjunction with potential restructuring activities. If we cannot successfully negotiate or renegotiate collective bargaining agreements, or if negotiations take an excessive amount of time, there may be a heightened risk of work stoppages. Work stoppages may be caused by the inability of national unions and the governments of countries in which the Company operates from reaching agreement, and are outside the control of the Company. Any work stoppage could have a material adverse effect on the productivity and profitability of a manufacturing facility or on our operations as a whole.

Increases in costs of pension benefits may reduce our profitability.

Our results of operations may be negatively affected by expenses we record for our defined benefit pension plans. Generally accepted accounting principles in the United States, or U.S. GAAP, require that we calculate income or expense for the plans using actuarial valuations. These valuations reflect assumptions about financial markets and other economic conditions, which may change based on changes in key economic indicators. We are required to make an annual measurement of plan assets and liabilities, which may result in increased funding obligations or negative changes in our stockholder equity. At the end of 2013, the combined projected benefit obligation of our U.S. and French pension and other postretirement healthcare plans was underfunded by $23.8 million. For a discussion regarding our pension obligations, see Note 16. Postretirement and Other Benefits of the Notes to Condensed Consolidated Financial Statements in Part II, Item 8 and Other Factors Affecting Liquidity and Capital Resources in Part II, Item 7. Although expense and pension funding contributions are not directly related, key economic factors that affect expense would also likely affect the amount of cash we would contribute to pension plans as required under the Employee Retirement Income Security Act (ERISA) for U.S. plans. Failure to achieve expected returns on plan assets driven by various factors, which could include a continued environment of low interest rates or sustained market volatility, could also result in an increase to the amount of cash we would be required to contribute to pension plans.

Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

As of December 31, 2013, we operated 14 production facilities (which include three fiber pulping operations) on four continents. In 2013, we acquired five facilities in our Filtration segment in connection with our acquisition of DelStar. The following are locations of our principal production facilities which are owned, except for the Strykow, Poland, Austin, Texas, Richland Pennsylvania, El Cajon, California and Suzhou, China facilities which are leased, as of December 31, 2013:

Paper Segment Production Locations	Reconstituted Tobacco Segment Production Locations	Filtration Segment Production Locations
Spotswood Mill Spotswood, New Jersey	LTR Industries Mill Spay, France	Middletown Manufacturing Site Middletown, Delaware
Papeteries de Saint-Girons Mill Saint-Girons, France	Ancram Mill Ancram, New York	U.S. Netting Austin, Texas
Papeteries de Mauduit Mill Quimperlé, France	RTL Philippines Mill (construction suspended) Sto. Tomas, Philippines	Tubing Operations Richland, Pennsylvania
Pirahy Mill Piraí, Brazil		Tubing Operations El Cajon, California
SWM-Poland Strykow, Poland		Suzhou Manufacturing Site Suzhou, China
Newberry Operation Newberry, South Carolina		
Fiber Operation Manitoba, Canada		

As of December 31, 2013, we had approximately 102,000 metric tons of annual paper production capacity and approximately 82,000 metric tons of annual reconstituted tobacco products production capacity, dependent upon the production mix. Capacity utilization increased in 2013 to 95% for paper products compared with 86% in 2012, while capacity utilization decreased to 92% for reconstituted tobacco products compared with 98% in 2012. Filtration product manufacturing lines operated at 74% capacity as of December 31, 2013. We also operate flax fiber processing operations in Canada and printing operations in France, Poland and the United States. We own each of these facilities and the associated operating equipment except for a flax tow storage facility in Winkler, Manitoba and the mill building in Strykow, Poland, which are leased.

We maintain administrative and sales offices in Alpharetta, Georgia, in Quimperlé and Spay, France, in Shanghai, China, in Piraí, Brazil, in Moscow, Russia, in Strykow, Poland, in Middletown, Delaware and in Bristol, England. Our world headquarters are also located in Alpharetta. All of these offices are owned except for those located in Alpharetta, Shanghai, Moscow, Bristol and Strykow which are leased.

We consider all of our facilities to be well-maintained, suitable for conducting our operations and business, and adequately insured, except for the RTL Philippines facility in Sto. Tomas, Philippines, which is being held in a mothballed state which would require additional construction work before operations commence.

Item 3. Legal Proceedings

General

We are involved in various legal proceedings relating to contracts, commercial disputes, taxes, environmental issues, employment and workers' compensation claims, product liability and other matters. We periodically review the status of these proceedings with both inside and outside counsel. We believe that the ultimate disposition of these matters will not have a material effect on the results of operations in a given quarter or year. Below is a summary of our major outstanding litigation.

Litigation

Imposto sobre Circulação de Mercadorias e Serviços, or ICMS, a form of value-added tax in Brazil, was assessed to our Brazilian subsidiary Schweitzer-Mauduit do Brasil Indústria e Comércio de Papel Ltda. in December of 2000. SWM-B received two assessments from the tax authorities of the State of Rio de Janeiro for unpaid ICMS taxes on certain raw materials from January 1995 through November 2000, collectively the Raw Materials Assessment.

The Raw Materials Assessment concerned the accrual and use by SWM-B of ICMS tax credits generated from the production and sale of certain non-tobacco related grades of paper sold domestically that are immune from the tax to offset ICMS taxes otherwise owed on the sale of products that are not immune. One of the two assessments, or Assessment 1 (case number 2001.001.115144-5), related in part to tax periods that predated our acquisition of the Pirahy mill in Pirai, Brazil and is covered in part by an indemnification from the sellers of the Pirahy mill. The second assessment, or Assessment 2 (case number 2001.001.064544-6), pertains exclusively to periods that SWM-B owned the Pirahy mill. While SWM-B would be primarily responsible for the full payment of the Assessment in the event of an ultimate unfavorable outcome, SWM-B is not aware of any difficulties that would be encountered in obtaining reimbursement of that portion of any payment resulting from Assessment 1 from the previous owners of the Pirahy mill under the indemnification.

SWM-B has contested the Raw Materials Assessment based on Article 150, VI of the Brazilian Federal Constitution of 1988, which grants immunity from ICMS taxes to papers used in the production of books, newspapers and periodicals, or immune papers, and the raw material inputs used to produce immune papers.

Both Raw Materials Assessments are presently on appeal in separate chambers of the Federal Supreme Court of Brazil. SWM-B won a favorable ruling in both assessments at the first level, then lost Assessment 1 on appeal and won Assessment 2 on appeal. Assessment 1 is before the court on SWM-B’s appeal of a procedural question which, if decided favorably, would invalidate Assessment 1. If decided against SWM-B, the lower court would be notified to send the case records to the Federal Supreme Court for a decision on the merits. Assessment 2 is before the Federal Supreme Court of Brazil on the State’s appeal on the merits and will be finally decided by the action of the chamber of the court hearing the matter, unless there is a prior decision by a chamber of the Federal Supreme Court on Assessment 1 that is in contradiction, in which case the conflict between the rulings of the different chambers would be decided by the Federal Supreme Court sitting as a whole. No docket entry has been made yet regarding argument on either assessment. Based on the foreign currency exchange rate at December 31, 2013, the Raw Materials Assessment totaled approximately $39 million, of which approximately $17 million is covered by the above-discussed indemnification.

More recently, SWM-B has received assessments from the tax authorities of the State of Rio de Janeiro for unpaid ICMS and Fundo Estadual de Combate à Pobreza (FECP) taxes on interstate purchases of electricity. The state issued three assessments against SWM-B, one for May 2006 - November 2007, a second for January 2008 - December 2010, and in October 2013, a third assessment for September 2011 - September 2013, collectively the Electricity Assessment. SWM-B has challenged all three Electricity Assessments in administrative proceedings before the state

tax council (Junta de Revisão Fiscal) based on Resolution 1.610/89, which defers these taxes on electricity purchased by an "electricity-intensive consumer."

SWM-B's challenges to the first two Electricity Assessments were unsuccessful at the first administrative level, but different appeals chambers of the Junta de Revisão Fiscal have reached different conclusions about the assessments. On the first electricity assessment, one chamber of the Junta de Revisão Fiscal recognized that SWM-B is an electricity-intensive consumer but denied applicability of the tax deferral resolution. The first assessment is now on appeal before the full council of the Junta de Revisão Fiscal. Court proceedings are possible if the full administrative council issues an adverse decision. On the second electricity assessment, SWM-B won a favorable ruling at the second administrative level, which recognized that SWM-B is an electricity-intensive consumer and agreed that the tax deferral resolution applies. SWM-B's challenge to the third electricity assessment is pending at the first administrative level. Based on the foreign currency exchange rate at December 31, 2013, the electricity assessments totaled approximately $19 million.

SWM-B continues to vigorously contest the Raw Materials Assessment and the Electricity Assessment and believes that the assessments will ultimately be resolved in its favor. No liability has been recorded in our condensed consolidated financial statements for these assessments based on our evaluation of these matters under the facts and law as presently understood.

Environmental Matters

The Company's operations are subject to various nations' federal, state and local laws, regulations and ordinances relating to environmental matters. The nature of the Company's operations exposes it to the risk of claims with respect to various environmental matters, and there can be no assurance that material costs or liabilities will not be incurred in connection with such claims. While the Company has incurred in the past several years, and will continue to incur, capital and operating expenditures in order to comply with environmental laws and regulations, it believes that its future cost of compliance with environmental laws, regulations and ordinances, and its exposure to liability for environmental claims and its obligation to participate in the remediation and monitoring of certain hazardous waste disposal sites, will not have a material effect on its financial condition or results of operations. However, future events, such as changes in existing laws and regulations, or unknown contamination of sites owned, operated or used for waste disposal by the Company (including contamination caused by prior owners and operators of such sites or other waste generators) may give rise to additional costs which could have a material effect on its financial condition or results of operations.

Indemnification Matters

In connection with our spin-off from Kimberly-Clark in 1995, we undertook to indemnify and hold Kimberly-Clark harmless from claims and liabilities related to the businesses transferred to us that were not identified as excluded liabilities in the related agreements. As of December 31, 2013, there are no material claims pending under this indemnification.

Item 4. Mine Safety Disclosures

Not applicable.

PART II.

Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

Market Information. Since November 30, 1995, our common stock, $0.10 par value per share, or Common Stock, has been listed on the New York Stock Exchange, trading under the symbol "SWM". On February 26, 2014, our stock closed at $47.41 per share.

The table below presents the high and low sales prices of our Common Stock on the New York Stock Exchange - Composite Transactions reporting system for the periods indicated.

	High	Low
2014		
First Quarter (through February 26, 2014)	$51.23	$42.53
2013		
Fourth Quarter	$63.53	$47.72
Third Quarter	61.63	48.95
Second Quarter	51.26	38.64
First Quarter	42.50	35.87
2012		
Fourth Quarter	$39.40	$32.03
Third Quarter	35.39	31.18
Second Quarter	35.49	32.01
First Quarter	36.50	30.59

Performance Graph. The following graph compares the total cumulative stockholder return on our Common Stock during the period from December 31, 2008 through December 31, 2013, with the comparable cumulative total returns of the Wilshire 5000 Index and a self-constructed peer group which reflects, but is not exactly comparable to, the Dow Jones Paper Products Index. We have selected the following companies as our peer group: Neenah Paper Inc., P.H. Glatfelter Co., and Wausau Paper Corp.

The graph assumes that the value of the investments in the Common Stock and each index were $100 on December 31, 2008 and that all dividends were reinvested. The returns of the companies in the peer group have been weighted according to their market capitalization. The stock price performance shown on the graph below is not necessarily indicative of future price performance.

Comparison of Cumulative Five Year Return
Holders. As of February 26, 2014, there were 2,197 stockholders of record.

Dividends. We have declared and paid cash dividends on our Common Stock every fiscal quarter since the second quarter of 1996. We announced in February 2014 a dividend of $0.36 per share payable on March 20, 2014 to stockholders of record on February 28, 2014. Our Credit Agreement covenants require that we maintain certain financial ratios, as disclosed in Note 12, Debt, of the Notes to Consolidated Financial Statements, none of which under normal business conditions materially limit our ability to pay such dividends. We will continue to assess our dividend policy in light of our cash generation, debt levels and ongoing requirements for cash to fund operations and to pursue possible strategic opportunities.

Recent Sales of Unregistered Securities. We had no unregistered sales of equity securities during the fiscal year ended December 31, 2013.

Repurchases of Equity Securities. The following table indicates the cost of and number of shares of the Company's common stock it has repurchased during 2013 and the remaining amount of share repurchases currently authorized by our Board of Directors as of December 31, 2013:

Issuer Purchases of Equity Securities

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Programs		Approximate Dollar Value of Shares that May Yet be Purchased Under the Programs
			(# shares)	($ in millions)	($ in millions)
First Quarter 2013	43,458	$38.03	—	$—	
Second Quarter 2013	—	—	—	$—	
Third Quarter 2013	—	—	—	$—	
October 2013	—	—	—	$—	
November 2013	—	—	—	$—	
December 2013	—	—	—	—	
Total 2013	43,458	$38.03	—	$—	$50.0

In September 2013, the Board of Directors authorized the repurchase of shares of SWM common stock during the period from November 8, 2013 to December 31, 2014 in an amount not to exceed $50.0 million. During 2014, 769,400 shares have been repurchased under this authorization for $35.0 through February 26, 2014.

The Company sometimes uses corporate 10b5-1 plans to allow for share repurchases to be made at predetermined stock price levels, without restricting such repurchases to specific windows of time. Future common stock repurchases will be dependent upon various factors, including the Company's stock price, strategic opportunities and cash availability.

Item 6. Selected Financial Data

The following selected financial data should be read in conjunction with Part II, Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations," and the consolidated financial statements and related notes within this Annual Report on Form 10-K. The results of our San Pedro, Philippines, Medan, Indonesia and Malaucène, France mills have been retrospectively presented as discontinued operations for all periods, the first two of which were sold in 2013. The results for 2013 include results of operations of DelStar, Inc. which was acquired on December 12, 2013. All dollar amounts are in millions except per share amounts, statistical data and ratios.

	For the Years Ended December 31,				
	2013	2012	2011	2010	2009
Results of Operations					
Net Sales	$772.8	$778.5	$788.3	$704.1	$689.7
Cost of products sold	520.1	519.0	545.3	511.8	507.6
Gross Profit	252.7	259.5	243.0	192.3	182.1
Nonmanufacturing expenses	86.5	86.4	88.0	71.3	71.9
Provision for losses on business tax credits	—	—	15.9	—	—
Restructuring & impairment expense	41.3	21.4	14.0	11.6	23.9
Operating Profit	124.9	151.7	125.1	109.4	86.3
Income from Continuing Operations	78.5	104.1	92.1	72.7	58.2
(Loss) income from Discontinued Operations	(2.4)	(24.3)	0.5	(7.4)	(22.6)
Net Income	$76.1	$79.8	$92.6	$65.3	$35.6
Net Income (Loss) Per Share- Basic:					
Income from continuing operations	$2.51	$3.33	$2.73	$2.00	$1.86
(Loss) income from discontinued operations	(0.08)	(0.79)	0.02	(0.20)	(0.72)
Net income per share - Basic	$2.43	$2.54	$2.75	$1.80	$1.14
Net Income (Loss) Per Share - Diluted:					
Income from continuing operations	$2.49	$3.29	$2.71	$1.96	$1.81
(Loss) income from discontinued operations	(0.07)	(0.78)	0.02	(0.20)	(0.71)
Net income per share - Diluted	$2.42	$2.51	$2.73	$1.76	$1.10
Cash Dividends Declared and Paid Per Share	$1.26	$0.45	$0.30	$0.30	$0.30
EBITDA from Continuing Operations[1]	$171.7	$195.4	$163.3	$145.1	$124.5
Adjusted EBITDA from Continuing Operations [1]	$213.0	$216.8	$193.2	$156.7	$148.4
Percent of Net Sales					
Gross Profit	32.7%	33.3%	30.8%	27.3%	26.4%
Nonmanufacturing expenses	11.2%	11.1%	11.2%	10.1%	10.4%
Financial Position					
Capital spending	$29.1	$27.2	$60.9	$73.7	$15.3
Depreciation and amortization	37.3	38.5	42.1	38.7	42.6
Total Assets	1,224.4	886.7	841.9	850.4	791.9
Total Debt	385.4	156.0	146	51.8	60.1
Total debt to capital ratio	40.7%	23.4%	23.5%	9.0%	11.1%

(1) Earnings before interest, taxes, depreciation and amortization (EBITDA) from Continuing Operations is a non-GAAP financial measure that is calculated by adding interest expense, income tax provision and depreciation and amortization expense to income from continuing operations, reduced by amortization of deferred revenue. Adjusted EBITDA from continuing operations is a non-GAAP financial measure that is calculated by adding restructuring and impairment expense and provision for losses on business tax credits to EBITDA from continuing operations. The Company believes investors' understanding of the Company's performance is enhanced by disclosing these non-GAAP financial measures as a reasonable basis for comparison of the Company's ongoing results of operations. Reconciliations to income from continuing operations are as follows ($ in millions):

	For the Years Ended December 31,				
	2013	2012	2011	2010	2009
Income from Continuing Operations	$78.5	$104.1	$92.1	$72.7	$58.2
Plus: Interest expense	2.9	3.3	2.3	1.6	4.0
Plus: Tax provision	53.0	49.5	32.8	39.3	24.8
Plus: Depreciation and amortization	37.3	38.5	42.1	38.7	42.6
Less: Amortization of deferred revenue	—	—	(6.0)	(7.2)	(5.1)
EBITDA from Continuing Operations	171.7	195.4	163.3	145.1	124.5
Plus: Provision for losses on business tax credits	—	—	15.9	—	—
Plus: Restructuring and impairment expense	41.3	21.4	14.0	11.6	23.9
Adjusted EBITDA from Continuing Operations	$213.0	$216.8	$193.2	$156.7	$148.4

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following is a discussion of our results of operations and financial condition. This discussion should be read in conjunction with our consolidated financial statements and related notes included elsewhere in this report and the selected financial data included in Item 6. The discussion of our results of operations and financial condition includes various forward-looking statements about our markets, the demand for our products and our future prospects. These statements are based on certain assumptions that we consider reasonable. For information about risks and exposures relating to us and our business, you should read the section entitled "Factors That May Affect Future Results," in Part I, Item 1A of this Annual Report on Form 10-K and our Forward Looking Statement Legend at the end of this Item 7. Unless the context indicates otherwise, references to "SWM", "we", "us", "our", or similar terms include Schweitzer-Mauduit International, Inc. and our consolidated subsidiaries.

This Management's Discussion and Analysis of Financial Condition and Results of Operation is designed to provide a reader of our financial statements with an understanding of our recent performance, our financial condition and our prospects. The following will be discussed and analyzed:

- Summary
- Recent Developments
- Critical Accounting Policies and Estimates
- Recent Accounting Pronouncements
- Results of Operations
- Liquidity and Capital Resources
- Other Factors Affecting Liquidity and Capital Resources
- Contractual Obligations
- Outlook
- Forward-Looking Statements

Summary

In 2013, SWM reported net income of $76.1 million on total net sales of $772.8 million. Compared to the prior year, net sales decreased $5.7 million due to the $21.9 million combined impact of lower volumes, price and mix, particularly in the Reconstituted Tobacco segment driven primarily by lower customer demand. This was partially offset by $13.2 million in foreign currency translation benefits and $4.2 million of revenue from DelStar, Inc. ("DelStar") which was acquired during the fourth quarter. Favorable currency benefits helped mitigate the revenue loss impact on operating profit and net income.

Cash provided by operations was $178.1 million in 2013 compared to $174.6 million in 2012. The $3.5 million increase was due primarily to a $4.0 million favorable year over year net change in working capital. Uses of cash during 2013 included $231.3 million to acquire DelStar, funded primarily through our credit facility, $29.1 million of capital spending and $39.5 million in cash dividends paid to SWM stockholders.

Return on invested capital (ROIC), adjusted to exclude the impact of restructuring-related costs, was 24.9 percent in 2013 compared to 23.5 percent in 2012. This measure reflects our determination to invest in products, projects and businesses that consistently yield returns in excess of our underlying cost of capital.

Recent Developments

On December 12, 2013, SWM acquired DelStar, Inc. or DelStar, a producer of specialty filtration materials, for $231.3 million, subject to customary post-closing adjustments. DelStar's suite of highly engineered resin materials, largely from filtration products such as reverse osmosis and other water filtration applications, are sold to a broad customer base in fast-growing water and industrial filtration segments. We believe the acquisition creates an attractive growth platform in an adjacent business area for SWM as we greatly expand our presence in advanced materials. In our discussion of results from operations in 2013, DelStar's results of operations since the closing are included in the Filtration segment.

In December 2013, we amended and restated our unsecured revolving credit facility, or Credit Agreement, to increase our borrowing capacity to $500 million. The increased borrowing capacity was used to pay for our acquisition of DelStar and other corporate uses. See Note 12. Debt, for additional information.

On November 6, 2013, SWM announced an increase of its quarterly dividend to $0.36 per share. The increase is part of SWM's long-term capital allocation strategy which is focused on investing in our core business, returning one-third of free cash flow to stockholders via dividends and share repurchases while retaining flexibility to explore growth and diversification opportunities, including in current and adjacent industries.

Construction progress continues on our facility at our reconstituted tobacco joint venture in China, China Tobacco-Schweitzer (Yunnan) Reconstituted Tobacco Company Ltd., or CTS, which is on track to open in 2014 with an expected ramp to full capacity by 2016. We expect CTS to incur additional start-up expenses in 2014 compared to 2013 and achieve profitable operations in 2015.

In December 2013, we recorded a $37.2 million non-cash impairment charge to reduce the carrying value of the Company's mothballed RTL-Philippines facility following decreased near term RTL volume expectations.

During 2013, SWM sold its paper mill sites in San Pedro, Philippines and Medan, Indonesia, whose results were classified as discontinued operations.

We are monitoring the scheduled vote of Russia's legislature expected in May 2014 on whether to require LIP standards.

Critical Accounting Policies and Estimates

Our consolidated financial statements are prepared in conformity with accounting principles generally accepted in the United States, which require management to make estimates that affect the amounts of revenues, expenses, assets and liabilities reported and disclosure of contingencies. Changes in these estimates could have a significant impact on our results of operations, financial position, or cash flows. We discussed with the Audit Committee of the Board of Directors the estimates and judgments made for each of the following items and our accounting for and presentation of these items in the accompanying financial statements:

Accounting for Income Taxes

We must make assumptions, judgments and estimates to determine our current provision for income taxes and also our deferred income tax assets and liabilities and any valuation allowance to be recorded against a deferred income tax asset. Our judgments, assumptions and estimates take into account our interpretation of current tax laws. Changes in tax law or our interpretation of tax laws could significantly impact the amounts provided for income taxes in our consolidated financial statements. Our assumptions, judgments and estimates relative to the value of a deferred tax asset take into account projections of the amount and category of future taxable income. Actual operating results and the underlying amount and category of income in future years could render our current assumptions, judgments and estimates of recoverable net deferred taxes inaccurate. Any of the assumptions, judgments and estimates mentioned above could cause our actual income tax obligations to differ from our estimates, thus materially impacting our financial position, results of operations and cash flows.

We have available net operating loss carryforwards, or NOLs, and other various tax credits in the jurisdictions in which we operate, for which we recorded deferred tax assets totaling $23.1 million and $4.1 million, respectively, as of December 31, 2013. We record and maintain income tax valuation allowances to reduce deferred tax assets to an amount we estimate will be realizable more likely than not. Our deferred tax asset valuation allowances are primarily the result of uncertainties regarding the future realization of recorded tax benefits on tax loss carryforwards for certain entities. As a result, at December 31, 2013, we had $20.3 million of valuation allowances against certain of the deferred tax assets.

Expiration periods vary for our NOLs depending on the tax laws governing the jurisdiction where the NOL was generated. Under current tax laws, remaining NOLs in France and Brazil carry forward indefinitely, and NOLs in Spain, and the Philippines expire in 15 years and 3 years, respectively, subsequent to the year generated. We have recorded a valuation allowance to fully reserve our net deferred tax assets in Brazil, since we believe that we will not generate sufficient taxable income in Brazil within an acceptable period of time given the annual utilization limitation of 30% of taxable income. We have also recorded a valuation allowance to fully reserve the net deferred tax asset balance in the Philippines as this operation has been sold and we do not believe we will generate sufficient taxable income to utilize these assets.

We expect sufficient future taxable income in France to fully utilize the respective French NOL carryforward deferred tax assets. The Company's assumptions, judgments and estimates relative to the valuation of these net deferred tax assets take into account available positive and negative evidence of realizability, including recent financial performance, the ability to realize benefits of restructuring and other recent actions, projections of the amount and category of future taxable income and tax planning strategies. Actual future operating results and the underlying amount and category of income in future periods could differ from the Company's current assumptions, judgments and estimates. Although realization is not assured, the Company believes it is more likely than not that these net deferred tax assets at December 31, 2013, will be realized. Future operating losses in Brazil and the paper operations in France could result in recording additional valuation allowances in a future period which could be material to our results of operations in the period that such valuation allowance was recorded. If at a future date, the Company determines that the weight of the positive evidence is not sufficient to overcome the negative evidence, additional valuation

allowances against these deferred tax assets to reduce the net deferred tax asset to an amount we believe will more likely than not be realizable would be recorded in the period such determination is made.

The Company was granted certain tax incentives in Poland for investment in a special economic zone. These incentives are in the form of credits granted in 2011 that are available to offset qualified taxable income through 2020. Based on granted incentives, commitments achieved, including maintaining certain employment levels, and qualified investment through December 31, 2013, the Company had a $2.3 million deferred tax asset at December 31, 2013 which has been partially reserved due to realignment of our legal entity structure and resulting change in taxable status of our Polish operations.

At December 31, 2013 and 2012, we had unrecognized tax benefits related to income taxes of $1.8 million and $1.8 million, respectively. Changes in tax laws or interpretations of tax laws or in our corporate structure, as well as outcomes of current and future audits conducted by foreign and domestic tax authorities, could materially impact the amounts provided for income taxes in our consolidated financial statements.

For additional information regarding income taxes and valuation allowances, see Note 15, Income Taxes, of the Notes to Consolidated Financial Statements.

Accounting for Contingencies

We accrue an estimated loss by taking a charge to income when the likelihood that a future event, such as a legal proceeding, will result in a loss or the incurrence of a liability is probable and the amount of loss can be reasonably estimated. We disclose material contingencies if there is at least a reasonable possibility that a loss has been incurred. In determining whether a loss should be accrued, we evaluate, among other factors, the degree of probability of an unfavorable outcome and the ability to make a reasonable estimate of the amount of loss. Changes in these factors could materially impact our results of operations, financial position, or our cash flows.

For further information, please see “Litigation” in Part I, Item 3, “Legal Proceedings” and Note 18, Commitments and Contingencies, of the Notes to Consolidated Financial Statements.

Property, Plant and Equipment Valuation

Paper manufacturing, which is our primary manufacturing process, is a capital intensive process. As a result, we make substantial investments in property, plant and equipment which are recorded at cost. Net property, plant and equipment comprised 32% of our total assets as of December 31, 2013. Property, plant and equipment is depreciated on the straight-line method over the estimated useful lives of the assets. Paper machines and related equipment are not subject to substantial technological changes rendering them obsolete and are generally depreciated over estimated useful lives of 20 years. In the United States, banded cigarette paper production assets at the Spotswood Mill are generally depreciated over estimated useful lives of 5 years. When indications of impairment exist, we assess the likelihood of recovering the cost of long-lived assets based on our expectation of future profitability and undiscounted cash flow of the related asset group. These factors, along with management's plans with respect to the operations, are considered in assessing the recoverability of property, plant and equipment. Changes in management's estimates and plans could significantly impact our results of operations, financial position or cash flows.

As a result of excess capacity in the tobacco-related papers industry and increased purchased material and operating costs experienced in the last several years, competitive selling prices for certain of our products are not sufficient to cover our costs with a reasonable margin. Such competitive pressures have resulted in downtime of certain paper machines and, in some cases, accelerated depreciation or impairment of certain equipment. Over the past five years, we have restructured our operations to improve our competitiveness and profitability. As a result, we incurred significant charges related to asset impairments, accelerated depreciation and employee severances. Due to the closure of our mill in Malaucène, France, the activities of Malaucène have been presented as a discontinued operation and as a result of filing for liquidation in December 2011, the financial position of Malaucène has been deconsolidated. The results of Company's Indonesian and Philippines paper mills, which were sold during 2013, have been retrospectively

presented as discontinued operations.

In 2011, the Company revised its Asian RTL expansion plans and suspended the construction of the Philippine greenfield site. Due to this change, the carrying value of partially constructed assets is evaluated for impairment at each reporting period by assessing the recoverability of the costs based on the undiscounted cash flows of the operation, likelihood of its reactivation and alternative uses for the equipment. The undiscounted cash flows were less than the carrying value of the assets. Management used significant judgment to develop assumptions, including forecasted sales volumes and projected operational performance. Based on an evaluation of the fair value at December 31, 2013, which used independent appraisals of certain assets, the Company recorded a $37.2 million impairment charge during 2013. The net book value of the RTL Philippines property, plant and equipment was $31.5 million as of December 31, 2013. During 2012, the Company expected a portion of the equipment would be sold to its RTL joint venture in China. As a result, that portion of the assets was determined to be a separate group of assets for purposes of the impairment analysis, and a separate impairment analysis was performed based on the expected cash flows of the projected sale and estimated costs to be incurred in connection with that sale. Based on the analysis that was performed, the expected proceeds net of the expected costs to be incurred was less than the carrying value of that equipment and an impairment loss of $3.1 million was recorded in 2012. As of December 31, 2012, that equipment was no longer expected to be sold and thus the equipment was included with the remainder of the assets as one group of assets again for purposes of the impairment analysis.

Management continues to evaluate how to operate our production facilities more effectively with reduced tobacco-related papers volumes. Further restructuring actions are possible that might require additional write-offs or accelerated depreciation of some equipment.

Business Combinations

Accounting for business combinations requires us to recognize, separately from goodwill, the assets acquired and the liabilities assumed (“net assets”) at their acquisition date fair values. Goodwill is measured as the excess of consideration transferred over the net assets acquired at their respective fair values as of the acquisition date. The estimated fair values are based upon quoted market prices and widely accepted valuation techniques, which require significant estimates and assumptions including, but not limited to, estimating future cash flows and developing appropriate discount rates. While we use our best estimates and assumptions to accurately value assets acquired and liabilities assumed at the acquisition date, our estimates are inherently uncertain and subject to refinement. As a result, during the measurement period, which may be up to one year from the acquisition date, we may record adjustments to the assets acquired and liabilities assumed with the corresponding adjustment to goodwill, based on new information obtained about the facts and circumstances that existed as of the acquisition date. Upon the conclusion of the measurement period or final determination of the values of net assets acquired, whichever comes first, any subsequent adjustments are recorded to our consolidated statements of operations. See Note 3, DelStar Acquisition, of the Notes to Consolidated Financial Statements for additional information.

Recent Accounting Pronouncements

For a discussion regarding recent accounting pronouncements, see “Recent Accounting Pronouncements” included in Note 2, Summary of Significant Accounting Policies, of the Notes to Consolidated Financial Statements.

Results of Operations

	For the Years Ended December 31,		
	2013 [1]	2012	2011
	($ in millions, except per share amounts)		
Net Sales	$772.8	$778.5	$788.3
Cost of products sold	520.1	519.0	545.3
Gross Profit	252.7	259.5	243.0
Selling expense	20.9	21.9	21.4
Research expense	15.3	9.9	9.2
General expense	50.3	54.6	57.4
Total nonmanufacturing expenses	86.5	86.4	88.0
Provision for losses on business tax credits	—	—	15.9
Restructuring and impairment expense	41.3	21.4	14.0
Operating Profit	124.9	151.7	125.1
Interest expense	2.9	3.3	2.3
Other income (expense), net	5.7	1.2	(2.6)
Income from Continuing Operations before Income Taxes and Income from Equity Affiliates	127.7	149.6	120.2
Provision for income taxes	53.0	49.5	32.8
Income from equity affiliates, net of income taxes	3.8	4.0	4.7
Income from Continuing Operations	78.5	104.1	92.1
(Loss) income from Discontinued Operations	(2.4)	(24.3)	0.5
Net Income	$76.1	$79.8	$92.6
Net Income (Loss) Per Share - Basic:			
Income per share from continuing operations	$2.51	$3.33	$2.73
(Loss) income per share from discontinued operations	(0.08)	(0.79)	0.02
Net income per share - basic	$2.43	$2.54	$2.75
Net Income (Loss) Per Share - Diluted:			
Income per share from continuing operations	$2.49	$3.29	$2.71
(Loss) income per share from discontinued operations	(0.07)	(0.78)	0.02
Net Income per share - diluted	$2.42	$2.51	$2.73

[1] Results during the year ended December 31, 2013 include the results of DelStar, Inc. since its acquisition on December 12, 2013.

Discontinued Operations

The results of the closed tipping mill in Malaucène, France, or Malaucène mill, the Medan, Indonesia mill, or Indonesia mill, and San Pedro, Philippines, or Philippines mill, have been classified as discontinued operations. As a result, all periods presented have been retrospectively recast to exclude the discontinued operations. During 2013, the Company sold its Indonesia mill and its Philippines mill. The 2013 loss from discontinued operations is primarily due to restructuring-related severance charges at the Philippines mill. The 2012 loss from discontinued operations is primarily due to an impairment charge on the long-lived assets of the Indonesia mill based on estimated future cash flows, being the expected selling price of the business, inventory write-downs, restructuring charges and asset impairment charges at the Philippines mill. During 2011, the Malaucène mill entered liquidation resulting in a loss of control for accounting consolidation purposes. The net deficit of Malaucène was removed from the consolidated accounts resulting in the 2011 recognition of a $6.4 million net gain. Malaucène's results of operations were included in the Company's discontinued operations through the date of the 2011 liquidation filing.

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Year Ended December 31, 2013 Compared with the Year Ended December 31, 2012

Net Sales
(dollars in millions)

	2013	2012	Change	Percent Change	Consolidated Sales Volume Change (Units)
Paper	$543.4	$545.0	$(1.6)	(0.3)%	2%
Reconstituted Tobacco	225.2	233.5	(8.3)	(3.6)	(10)
Filtration	4.2	—	4.2	N.M.	N.M.
Total	$772.8	$778.5	$(5.7)	(0.7)%	(3)%

N.M. Not Meaningful

Net sales were $772.8 million in 2013 compared with $778.5 million in 2012. The decrease in net sales consisted of the following (dollars in millions):

	Amount	Percent
Changes in product mix and selling prices	$(25.9)	(3.3)%
Changes due to royalty income	(1.2)	(0.1)
Changes due to sales volume	4.0	0.5
Filtration segment revenue	4.2	0.5
Changes in currency exchange rates	13.2	1.7
Total	$(5.7)	(0.7)%

Total unit sales volumes decreased by 3% in the year ended December 31, 2013 versus the prior year.
Sales volumes for the Paper segment increased by 2%
Sales volumes for the Reconstituted Tobacco segment decreased by 10%

The Paper segment net sales during the year ended December 31, 2013 of $543.4 million decreased by $1.6 million, or 0.3%, versus $545.0 million in the prior year. The decrease in net sales was primarily the result of unfavorable product mix and changes in selling prices of $34.0 million and lower royalty revenue of $1.2 million. These unfavorable impacts were partially offset by $25.0 million favorable effect of higher volumes, including non-tobacco papers, and $8.6 million in favorable currency exchange.

The Reconstituted Tobacco segment net sales during the year ended December 31, 2013 of $225.2 million decreased by $8.3 million, or 3.6%, compared with $233.5 million in the prior-year period. The decrease in net sales of the Reconstituted Tobacco segment resulted from the $21.0 million impact of lower volumes which was partially offset by $8.1 million in favorable average selling prices resulting from the mix of products sold and $4.6 million of favorable currency impacts.

The Filtration segment net sales were $4.2 million for the 2013 period since the closing of the DelStar acquisition on December 12, 2013.

Operating Expenses
(dollars in millions)

	2013	2012	Change	Percent Change	Percent of Net Sales 2013	Percent of Net Sales 2012
Net Sales	$772.8	$778.5	$(5.7)	(0.7)%	100.0 %	100.0 %
Cost of products sold	520.1	519.0	1.1	0.2	67.3	66.7
Gross Profit	$252.7	$259.5	$(6.8)	(2.6)%	32.7 %	33.3 %

The $6.8 million decrease in gross profit during the year ended December 31, 2013 versus the prior year was primarily due to the $13.7 million negative impact of lower volume, $6.0 million from an unfavorable mix of products sold which included more non-tobacco volumes, and $3.7 million of higher wood pulp costs. The negative impacts were partially offset by $8.0 million in favorable currency translation, $6.6 million in savings from other costs of sales, including the Company's operational excellence program and $3.9 million in favorable energy, labor and other materials costs.

Nonmanufacturing Expenses
(dollars in millions)

	2013	2012	Change	Percent Change	Percent of Net Sales 2013	Percent of Net Sales 2012
Selling expense	$20.9	$21.9	$(1.0)	(4.6)%	2.7 %	2.8 %
Research expense	15.3	9.9	5.4	54.5	2.0	1.3
General expense	50.3	54.6	(4.3)	(7.9)	6.5	7.0
Nonmanufacturing expenses	$86.5	$86.4	$0.1	0.1 %	11.2 %	11.1 %

Nonmanufacturing expenses in the year ended December 31, 2013 increased by $0.1 million to $86.5 million from $86.4 million in the prior year due to higher expenditures on product diversification and growth initiatives which were partially offset by lower incentive compensation expenses.

Restructuring and Impairment Expense

The Company incurred total restructuring and impairment expense of $41.3 million in the year ended December 31, 2013, primarily due to a $37.2 million impairment charge to reduce the carrying value of the Company's mothballed RTL-Philippines facility following decreased near term RTL volume expectations. Other 2013 restructuring expenses included $2.7 million of severance and early retirement expenses in the French operations for ongoing accruals over the remaining service lives of affected employees associated with previously announced actions and $0.7 million of termination fees to exit third-party service contracts in the U.S. and Europe.

In the year ended December 31, 2012, the Company's restructuring and impairment expense of $21.4 million primarily included the following:

- $16.9 million for an impairment charge to reduce the carrying value of the Company's Spotswood, New Jersey mill, which produces banded cigarette paper, following the amendment of the Company's supply agreement with Philip Morris USA, a subsidiary of Altria Group Inc.,

- $3.7 million of charges in connection with the RTL Philippines site where construction was suspended, of which $3.1 million represented a non-cash impairment charge on certain of the equipment,

- $1.6 million of costs to terminate a third-party printing agreement in the U.S. in conjunction with a restructuring of the U.S. LIP business, and

- $2.4 million of severance and early retirement expenses in the French operations for ongoing accruals over the remaining service lives of affected employees related to previously announced actions.

Partially offsetting these expenses was a benefit of $2.5 million reversal of previously recorded special termination charges as a result of a change to French retirement laws during 2012 allowing earlier retirements for qualified workers, which will result in qualified workers receiving their government benefits earlier and, therefore, the workers will be paid less from the Company's early retirement plan.

Operating Profit
(dollars in millions)

	2013	2012	Change	Percent Change	Return on Net Sales 2013	Return on Net Sales 2012
Paper	$102.5	$84.4	$18.1	21.4 %	18.9 %	15.5 %
Reconstituted Tobacco	46.4	90.3	(43.9)	(48.6)	20.6	38.7
Filtration	(1.1)	—	(1.1)	N.M.	(26.2)%	N.M.
Unallocated expenses	(22.9)	(23.0)	0.1			
Total	$124.9	$151.7	$(26.8)	(17.7)%	16.2 %	19.5 %

N.M. - Not meaningful

Operating profit was $124.9 million in the year ended December 31, 2013 compared with $151.7 million during the prior year.

The Paper segment's operating profit in the year ended December 31, 2013 was $102.5 million, an increase of $18.1 million from the prior year. The increase was primarily due to the following factors:

- $15.5 million in lower restructuring and impairment expense primarily due to the $16.9 million Spotswood impairment charge during the first quarter of 2012;

- $6.0 million in favorable currency impacts; and

- $4.2 million improved inflationary costs, primarily other materials prices.

These positive factors were partially offset by $10.3 million in unfavorable mix of products sold and changes in average selling prices, $3.7 million in higher wood pulp costs, a $3.0 million impact from volume and $1.2 million of lower royalty income.

The Reconstituted Tobacco segment's operating profit in the year ended December 31, 2013 was $46.4 million compared to $90.3 million in the prior year. The decrease was primarily due to a $37.2 million non-cash impairment charge on the RTL-Philippines facility, $10.7 million unfavorable impact of lower volumes and $2.8 million unfavorable fixed cost absorption due to lower production volumes partially offset by $3.8 million in improved pricing and favorable mix of products sold.

Non-Operating Expenses

Interest expense was $2.9 million in the year ended December 31, 2013, a decrease from $3.3 million in the year ended December 31, 2012. The decrease in interest expense is primarily due to lower interest rates and lower average debt balances in 2013 versus 2012. The weighted average effective interest rates on our debt facilities were approximately 1.5% and 1.6% for the years ended December 31, 2013 and 2012, respectively.

Other income, net was $5.7 million during the year ended December 31, 2013 compared to $1.2 million during the year ended December 31, 2011. The $4.5 million increase in other income, net is due to higher foreign currency transaction gains and interest income.

Income Taxes

A $53.0 million provision for income taxes in the year ended December 31, 2013 resulted in an effective tax rate of 41.5% compared with 33.1% in the prior year. In the year ended December 31, 2013, the effective tax rate was higher than the 35% statutory rate due primarily to the impairment expenses incurred by the RTL Philippines facility that did not have any income tax benefits and recording a valuation allowance on a portion of Polish deferred tax assets which may not be realized as part of our legal entity realignment. During 2012, the 33.1% effective tax rate was lower than the 35% statutory rate due to lower income tax rates in Poland; however, this favorable impact was partially offset by losses and restructuring expenses incurred by the RTL Philippines facility that did not have any income tax benefits.

Income from Equity Affiliates

Income from equity affiliates was $3.8 million in the year ended December 31, 2013 compared with $4.0 million during the prior year. These results reflected the operations of the joint venture in China to produce cigarette papers, CTM, and expenses of the Chinese reconstituted tobacco joint venture, CTS, which is currently under construction.

Discontinued Operations

Due to our decisions to sell our Indonesia mill and our Philippines mill, the results of these entities were reported as discontinued operations for all periods presented. Consequently, their results have been removed from each line of the statements of income and the operating activities section of the statements of cash flow. In each case, a separate line has been added for the net results of the discontinued operation, including previously reported restructuring and impairment amounts. During 2013, the Company completed the sale of the Indonesia mill and Philippines mill and incurred a $1.6 million loss and $1.6 million gain on the sales, respectively, which are presented in discontinued operations.

Net Income and Income per Share

Net income in the year ended December 31, 2013 was $76.1 million, or $2.42 per diluted share, compared with $79.8 million, or $2.51 per diluted share, during the prior year. The decrease in net income was primarily due to $19.9 million of higher restructuring and impairment expenses and lower reconstituted tobacco volumes, partially offset by decreased losses from discontinued operations and operational excellence manufacturing improvements.

Year Ended December 31, 2012 Compared with the Year Ended December 31, 2011

Net Sales
(dollars in millions)

	2012	2011	Change	Percent Change	Consolidated Sales Volume Change (Units)
Paper	$545.0	$551.4	$(6.4)	(1.2)%	(4)%
Reconstituted Tobacco	233.5	236.9	(3.4)	(1.4)	6
Total	$778.5	$788.3	$(9.8)	(1.2)%	—%

Net sales were $778.5 million in 2012 compared with $788.3 million in 2011. The decrease in net sales consisted of the following (dollars in millions):

	Amount	Percent
Changes in currency exchange rates	$(55.9)	(7.1)%
Changes due to royalty income	(4.6)	(0.5)
Changes in product mix and selling prices	12.9	1.6
Changes due to volume	37.8	4.8
Total	$(9.8)	(1.2)%

- Changes in currency exchange rates decreased net sales by $55.9 million, or 7.1% , in 2012, and primarily reflected the impact of changes in the value of the euro compared with the U.S. dollar in 2012 versus the prior year.

- Royalty revenue decreased by $4.6 million in 2012 primarily due to the initiation of the license agreement during 2011 for which prior-period royalties were received.

- Favorable changes in average selling prices and mix of products sold increased net sales by $12.9 million.

- Total unit sales volumes were unchanged in 2012 versus the prior year.
  Sales volumes for the Paper segment decreased by 4%
  Sales volumes for the Reconstituted Tobacco segment increased by 6%

Paper segment net sales during the year ended December 31, 2012 of $545.0 million decreased by $6.4 million, or 1.2%, compared with $551.4 million in the prior year. The decrease in net sales was primarily the result of $39.5 million in unfavorable foreign exchange impacts mostly due to changes in the value of the euro compared to the U.S. dollar and $4.6 million impact from lower royalty revenue. These negative impacts were partially offset by a $22.7 million favorable impact of higher sales volumes, $13.2 million favorable impact of average selling prices and mix of products sold and $1.8 million tax credit gain recognized upon successful legal resolution of a business tax case in Brazil.

Reconstituted Tobacco segment net sales during the year ended December 31, 2012 of $233.5 million decreased by $3.4 million, or 1.4%, compared with $236.9 million in the prior year. The decrease in net sales of the Reconstituted Tobacco segment resulted from the unfavorable $16.4 million unfavorable foreign exchange impacts mostly due to changes in the value of the euro compared to the U.S. dollar which was partially offset by a $12.8 million favorable impact of higher sales volumes.

Operating Expenses
(dollars in millions)

	2012	2011	Change	Percent Change	Percent of Net Sales 2012	Percent of Net Sales 2011
Net Sales	$778.5	$788.3	$(9.8)	(1.2)%	100.0 %	100.0 %
Cost of products sold	519.0	545.3	(26.3)	(4.8)	66.7	69.2
Gross Profit	$259.5	$243.0	$16.5	6.8 %	33.3 %	30.8 %

The $16.5 million increase in gross profit during 2012 compared with the prior year was primarily due to the $29.2 million favorable impact of higher sales volumes and average selling prices, including mix of products sold. LIP regulations in the EU, which became effective during the fourth quarter of 2011, drove higher demand for LIP cigarette papers. Our operational excellence program generated approximately $27 million of cost savings during the year; however, those benefits were substantially offset by operational inefficiencies in certain locations as well as increases in inflationary costs and unfavorable currency impacts. Start-up costs during 2011 in Poland were not repeated during 2012. Pulp list prices were lower during 2012 at an average of $860 per metric ton of northern bleached softwood kraft compared to $980 per metric ton during the prior year. However, changes in pulp prices had a negligible impact on the comparison of 2012 and 2011 results. Changes in inflationary costs, including other materials prices, energy and labor, had an unfavorable impact of $11.4 million on 2012 results compared to the prior year. Changes in currency exchange rates unfavorably impacted the gross profit comparison by $7.2 million primarily from the weaker euro compared to the U.S. dollar. Royalty income was lower in 2012 by $4.6 million.

Nonmanufacturing Expenses
(dollars in millions)

	2012	2011	Change	Percent Change	Percent of Net Sales 2012	Percent of Net Sales 2011
Selling expense	21.9	21.4	$0.5	2.3 %	2.8 %	2.7 %
Research expense	9.9	9.2	0.7	7.6	1.3	1.2
General expense	54.6	57.4	(2.8)	(4.9)	7.0	7.3
Nonmanufacturing expenses	$86.4	$88.0	$(1.6)	(1.8)%	11.1 %	11.2 %

Nonmanufacturing expenses in 2012 decreased by $1.6 million to $86.4 million from $88.0 million in the prior year primarily due to lower legal expenses to defend the Company's LIP patents partially offset by higher transaction-related and strategic initiative expenses.

Provision for Losses on Business Tax Credits

During 2011, the Company recorded a $15.9 million charge to fully reserve the carrying value of its Imposto sobre Circulação de Mercadorias e Serviços, or ICMS, business tax credits in Brazil.

Restructuring and Impairment Expense

The Company incurred total restructuring and impairment expense of $21.4 million in 2012, which included the following:

- $16.9 million for an impairment charge to reduce the carrying value of the Company's Spotswood, New Jersey mill, which produces banded cigarette paper, following an amendment of the Company's supply agreement with Philip Morris USA, a subsidiary of Altria Group Inc.;

- $3.7 million of charges in connection with the RTL Philippines site where construction was suspended, of which $3.1 million represented a non-cash impairment charge on certain of the equipment;

- $1.6 million of costs to terminate a third-party printing agreement in the U.S. in conjunction with a restructuring of the U.S. LIP business; and

- $2.4 million of severance and early retirement expenses in the French operations for ongoing accruals over the remaining service lives of affected employees related to previously announced actions.

Partially offsetting these expenses was a benefit of $2.5 million reversal of previously recorded special termination charges as a result of a change to French retirement laws during 2012 allowing earlier retirements for qualified workers, which will result in qualified workers receiving their government benefits earlier and, therefore, the workers will be paid less from the Company's early retirement plan.

In 2011, the Company's restructuring and impairment expense was $14.0 million, which included $5.8 million in the Paper segment for employee severances and other cash costs and $3.6 million of impairment charges on property, plant and equipment. In the Reconstituted Tobacco segment, the Company incurred $4.6 million of impairment and other costs in 2011 related to the suspended construction of the RTL facility in the Philippines.

Operating Profit
(dollars in millions)

	2012	2011	Change	Percent Change	Return on Net Sales 2012	Return on Net Sales 2011
Paper	$84.4	$54.8	$29.6	54.0 %	15.5 %	9.9 %
Reconstituted Tobacco	90.3	90.3	—	—	38.7	38.1
Unallocated expenses	(23.0)	(20.0)	(3.0)			
Total	$151.7	$125.1	$26.6	21.3 %	19.5 %	15.9 %

Operating profit was $151.7 million in 2012 compared with $125.1 million during the prior year.

The Paper segment's 2012 operating profit was $84.4 million, an increase of $29.6 million from the prior year. The increase was primarily due to the following factors:

- $31.6 million in favorable impacts from higher sales volumes, substantially all from certain value-added products;

- $15.9 million in lower provision for losses on business tax credits;

- Lower non-manufacturing expenses, primarily due to approximately $9 million less in litigation expenses; and

- A tax credit gain of $1.8 million recognized upon successful legal resolution of a Brazil business tax case.

These positive factors were partially offset by a $10.1 million impact from lower average selling prices and an unfavorable mix of products sold, $8.5 million in higher restructuring and impairment expense, $8.4 million in increased inflationary costs primarily related to other materials, and $4.6 million of lower royalty income.

The Reconstituted Tobacco segment's 2012 operating profit was $90.3 million, unchanged from the prior year. The offsetting changes were primarily due to the following:

- $6.7 million in higher sales volume impacts; and
- $2.0 million in improved manufacturing impacts.

These positives were mostly offset by $6.4 million in unfavorable currency impacts and $2.1 million in higher inflationary costs

Non-Operating Expenses

Interest expense was $3.3 million in 2012, an increase from $2.3 million in 2011. The increase in interest expense is primarily due to lower capitalized interest in 2012. The Company capitalized $1.5 million of interest expense in 2011 related to the construction of the RTL facility in the Philippines and EU LIP facility in Poland. The weighted average effective interest rates on our debt facilities were approximately 1.6% and 2.0% for 2012 and 2011, respectively.

Other income, net was $1.2 million during 2012 due to foreign currency transaction gains and interest income. During 2011, other expense, net was $2.6 million primarily due to foreign exchange losses net of interest income.

Income Taxes

A $49.5 million provision for income taxes in 2012 resulted in an effective tax rate of 33.1% compared with 27.3% in the prior year. The effective tax rates were lower than the 35% statutory rate due primarily to the Company's Polish operations which were granted certain tax incentives for investment in a special economic zone. These incentives were in the form of credits that are used to offset qualified taxable income. Based on granted incentives, commitments achieved, including maintaining certain employment levels and qualified investment, the Company had available credits for which we recorded deferred income tax benefits. These credits had a remaining balance of $7.7 million at December 31, 2012. In 2011, the Company recorded a $5.9 million valuation allowance to fully reserve its net deferred tax assets in Brazil.

Income from Equity Affiliates

Income from equity affiliates was $4.0 million in 2012 compared with $4.7 million during the prior year. These results reflected the operations of CTM and expenses of CTS, which is currently under construction.

Discontinued Operations

Due to our decisions to sell our Indonesia mill and our Philippines mill, the results of these entities were reported as discontinued operations for all periods presented. Consequently, their results have been removed from each line of the statements of income and the operating activities section of the statements of cash flow. In each case, a separate line has been added for the net results of the discontinued operation, including previously reported restructuring and impairment amounts. During the fourth quarter of 2011, a liquidation petition relating to the Malaucène mill resulted in a loss of control. Consequently, consolidated results for 2012 do not include that entity's results.

Net Income and Income per Share

Net income in 2012 was $79.8 million, or $2.51 per diluted share, compared with $92.6 million, or $2.73 per diluted share, during the prior year. The decrease in net income was primarily due to losses from discontinued operations and a lower 2011 effective tax rate primarily as a result of the deferred income tax benefit recorded in 2011 to recognize Poland special economic zone credits.

Liquidity and Capital Resources

The Company has created a long-term capital allocation strategy which is focused on the following three areas:

- Reinvest capital in core businesses through a disciplined approach to meet global demand for value-adding solutions,

- Return at least one-third of annual free cash flow to stockholders via balanced dividends and share repurchase programs, and

- Retain flexibility to explore growth opportunities in current and adjacent markets with economic returns similar to or better than SWM's existing business.

A major factor in our liquidity and capital resource planning is our generation of cash flow from operations, which is sensitive to changes in the sales mix, volume and pricing of our products, as well as changes in our production volumes, costs and working capital. Our liquidity is supplemented by funds available under our revolving credit facility with a syndicate of banks that is used as either operating conditions or strategic opportunities warrant.

As of December 31, 2013, $267.3 million of the Company's $272.0 million of cash and cash equivalents was held by foreign subsidiaries. Movement of cash balances may have significant tax consequences. The Company considers the undistributed earnings of its foreign subsidiaries to be indefinitely reinvested and currently plans to repatriate such earnings only when tax effective to do so. We believe that we are able to maintain a sufficient level of liquidity for our domestic operations and commitments without repatriation of the cash held by these foreign subsidiaries. Certain legal entity realignments and other activities are underway that could permit tax effective repatriation of certain of these funds.

Capital spending for 2014 is projected to be approximately $25 million to $30 million. We generally fund our capital projects using cash on-hand, cash generated from operations and our existing credit facilities.

Cash Requirements

As of December 31, 2013, we had net operating working capital of $115.3 million and cash and cash equivalents of $272.0 million, compared with net operating working capital of $94.6 million and cash and cash equivalents of $151.2 million as of December 31, 2012. The 2013 year over year increase in net operating working capital is primarily due to the acquisition of DelStar in December 2013 and recording the fair value of the acquired assets and liabilities. Changes in these amounts reflect the impacts of changes in currency exchange rates and excess tax benefits of stock-based awards which are not included in the changes in operating working capital presented on the consolidated statements of cash flow.

Cash Flows from Operating Activities($ in millions)	For the Years Ended December 31,		
	2013	2012	2011
Net Income	$76.1	$79.8	$92.6
Less: (Loss) income from discontinued operations	(2.4)	(24.3)	0.5
Income from continuing operations	78.5	104.1	92.1
Non-cash items included in net income:			
Depreciation and amortization	37.3	38.5	42.1
Impairment	37.2	20.2	6.8
Provision for losses on business tax credits	—	—	15.9
Amortization of deferred revenue	—	—	(6.0)
Deferred income tax provision (benefit)	17.3	13.1	(13.9)
Pension and other postretirement benefits	1.1	1.0	(6.5)
Stock-based compensation	3.2	6.9	3.8
Income from equity affiliates	(3.8)	(4.0)	(4.7)
Excess tax benefits of stock-based awards	(0.5)	(1.4)	(10.0)
Cash dividends received from equity affiliates	3.7	3.0	—
Other items	1.0	(0.1)	(3.1)
Net changes in operating working capital	0.8	(3.2)	(25.1)
Net cash provided (used) by operating activities of:			
Continuing operations	175.8	178.1	91.4
Discontinued operations	2.3	(3.5)	(9.9)
Cash Provided by Operations	$178.1	$174.6	$81.5

Net cash provided by operations was $178.1 million in the year ended December 31, 2013 compared with $174.6 million in the prior year. Our net cash provided by operations increased due to a favorable net change in working capital.

Net cash provided by operations was $174.6 million in 2012 compared with $81.5 million in 2011. Our net cash provided by operations changed favorably by $93.1 million in 2012 compared to the prior year primarily due to increased profitability net of non-cash impairment charges and deferred income taxes, and a favorable net change in working capital.

Operating Working Capital($ in millions)	For the Years Ended December 31,		
	2013	2012	2011
Changes in operating working capital			
Accounts receivable	$4.4	$14.3	$(25.8)
Inventories	(1.0)	(6.1)	(5.9)
Prepaid expenses	0.1	(1.0)	0.4
Accounts payable	(1.5)	(7.0)	(3.5)
Accrued expenses	3.4	(8.1)	1.5
Accrued income taxes	(4.6)	4.7	8.2
Net changes in operating working capital	$0.8	$(3.2)	$(25.1)

In 2013, net changes in operating working capital provided cash flow of $0.8 million. The 2013 favorable change in working capital was driven by the collection of certain advance payments during late 2012, timing of purchases versus payments of accounts payable, as well as timing of income tax installments.

In 2012, net changes in operating working capital were unfavorable to cash flow by $3.2 million primarily driven by improved receivable collection and timing of payments.

In 2011, net changes in operating working capital contributed unfavorably to cash flow by $25.1 million. The change in working capital was primarily driven by initiation of operations in Poland to support European LIP sales.

Cash Flows from Investing Activities($ in millions)	For the Years Ended December 31,				
	2013		2012		2011
Capital spending	$(29.1	)	$(27.2	)	$(60.9