

Edgar Filing: Clearwater Paper Corp - Form 10-Q

Clearwater Paper Corp
Form 10-Q
August 07, 2018

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

Form 10-Q
(Mark One)

Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the quarterly period ended June 30, 2018

or
 Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the transition period from _____ to _____

Commission File Number: 001-34146

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

Delaware 20-3594554
(State or other jurisdiction of (I.R.S. Employer
incorporation or organization) Identification No.)

601 West Riverside, Suite 1100 99201
Spokane, Washington
(Address of principal executive offices) (Zip Code)
(509) 344-5900
(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (section 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

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

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

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

The number of shares of common stock of the registrant outstanding as of August 3, 2018 was 16,461,119.

CLEARWATER PAPER CORPORATION
Index to Form 10-Q

	Page Number
PART I. <u>FINANCIAL INFORMATION</u>	
ITEM 1. <u>Consolidated Financial Statements</u>	
<u>Consolidated Statements of Operations for the three and six months ended June 30, 2018 and 2017</u>	<u>2</u>
<u>Consolidated Statements of Comprehensive Income for the three and six months ended June 30, 2018 and 2017</u>	<u>3</u>
<u>Consolidated Balance Sheets at June 30, 2018 and December 31, 2017</u>	<u>4</u>
<u>Condensed Consolidated Statements of Cash Flows for the six months ended June 30, 2018 and 2017</u>	<u>5</u>
<u>Condensed Notes to Consolidated Financial Statements</u>	<u>6 - 23</u>
ITEM 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>24 - 35</u>
ITEM 3. <u>Quantitative and Qualitative Disclosures About Market Risk</u>	<u>35</u>
ITEM 4. <u>Controls and Procedures</u>	<u>35</u>
PART II. <u>OTHER INFORMATION</u>	
ITEM 1. <u>Legal Proceedings</u>	<u>36</u>
ITEM 1A. <u>Risk Factors</u>	<u>36</u>
ITEM 2. <u>Unregistered Sales of Equity Securities and Uses of Proceeds</u>	<u>36</u>
ITEM 6. <u>Exhibits</u>	<u>37</u>
<u>SIGNATURES</u>	<u>38</u>

Part I
 ITEM 1.
 Consolidated
 Financial
 Statements
 Clearwater Paper Corporation
 Consolidated Statements of Operations
 Unaudited (Dollars in thousands - except per-share amounts)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2018	2017	2018	2017
Net sales	\$432,099	\$429,663	\$869,051	\$867,188
Costs and expenses:				
Cost of sales	(387,154)	(381,061)	(779,587)	(768,121)
Selling, general and administrative expenses	(26,564)	(29,454)	(59,544)	(59,409)
Total operating costs and expenses	(413,718)	(410,515)	(839,131)	(827,530)
Income from operations	18,381	19,148	29,920	39,658
Interest expense, net	(7,723)	(7,673)	(15,743)	(15,716)
Non-operating pension and other postretirement benefit (costs) income	(1,187)	517	(2,466)	565
Earnings before income taxes	9,471	11,992	11,711	24,507
Income tax provision	(2,510)	(3,955)	(2,150)	(8,955)
Net earnings	\$6,961	\$8,037	\$9,561	\$15,552
Net earnings per common share:				
Basic	\$0.42	\$0.49	\$0.58	\$0.94
Diluted	0.42	0.48	0.58	0.94

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

Clearwater Paper Corporation
 Consolidated Statements of Comprehensive Income
 Unaudited (Dollars in thousands)

	Three Months Ended		Six Months Ended	
	June 30,		June 30,	
	2018	2017	2018	2017
Net earnings	\$6,961	\$8,037	\$9,561	\$15,552
Other comprehensive income:				
Defined benefit pension and other postretirement employee benefits:				
Amortization of actuarial loss included in net periodic cost, net of tax of \$588, \$234, \$1,205 and \$648	1,644	357	3,372	988
Amortization of prior service credit included in net periodic cost, net of tax of \$(111), \$(151), \$(221) and \$(302)	(308)	(231)	(617)	(461)
Other comprehensive income, net of tax	1,336	126	2,755	527
Comprehensive income	\$8,297	\$8,163	\$12,316	\$16,079

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

Clearwater Paper Corporation
Consolidated Balance Sheets
Unaudited (Dollars in thousands – except per-share amounts)

	June 30, 2018	December 31, 2017
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 53,278	\$ 15,738
Receivables, net	118,726	142,065
Taxes receivable	8,784	20,282
Inventories	262,213	266,043
Other current assets	8,132	8,661
Total current assets	451,133	452,789
Property, plant and equipment, net	1,171,368	1,050,982
Goodwill	244,161	244,161
Intangible assets, net	28,642	32,542
Other assets, net	24,093	21,778
TOTAL ASSETS	\$ 1,919,397	\$ 1,802,252
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Borrowings under revolving credit facilities	\$ 160,000	\$ 155,000
Accounts payable and accrued liabilities	357,588	256,621
Current liability for pensions and other postretirement employee benefits	7,631	7,631
Total current liabilities	525,219	419,252
Long-term debt	570,908	570,524
Liability for pensions and other postretirement employee benefits	69,504	72,469
Other long-term obligations	37,734	43,275
Accrued taxes	3,116	2,770
Deferred tax liabilities	122,347	118,528
TOTAL LIABILITIES	1,328,828	1,226,818
Stockholders' equity:		
Preferred stock, par value \$0.0001 per share, 5,000,000 authorized shares, no shares issued	—	—
Common stock, par value \$0.0001 per share, 100,000,000 authorized shares-16,461,119 and 16,447,898 shares issued	2	2
Additional paid-in capital	3,980	1,161
Retained earnings	640,667	618,254
Accumulated other comprehensive loss, net of tax	(54,080) (43,983
TOTAL STOCKHOLDERS' EQUITY	590,569	575,434
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$ 1,919,397	\$ 1,802,252

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

Clearwater Paper Corporation
Condensed Consolidated Statements of Cash Flows
Unaudited (Dollars in thousands)

	Six Months Ended June 30,	
	2018	2017
CASH FLOWS FROM OPERATING ACTIVITIES		
Net earnings	\$9,561	\$15,552
Adjustments to reconcile net earnings to net cash flows from operating activities:		
Depreciation and amortization	50,344	53,612
Deferred taxes	2,649	7,891
Employee benefit plans	326	(2,183)
Deferred issuance costs on debt	716	598
Other non-cash adjustments, net	427	1,072
Changes in working capital, net	36,317	23,742
Changes in taxes receivable, net	11,498	4,229
Other, net	(962)	(914)
Net cash flows from operating activities	110,876	103,599
CASH FLOWS FROM INVESTING ACTIVITIES		
Additions to property, plant and equipment	(78,600)	(85,709)
Other, net	807	417
Net cash flows from investing activities	(77,793)	(85,292)
CASH FLOWS FROM FINANCING ACTIVITIES		
Purchase of treasury stock	—	(4,875)
Borrowings on revolving credit facilities	124,063	117,000
Repayments of borrowings on revolving credit facilities	(119,063)	(144,000)
Other, net	(543)	(914)
Net cash flows from financing activities	4,457	(32,789)
Increase (decrease) in cash and cash equivalents	37,540	(14,482)
Cash and cash equivalents at beginning of period	15,738	23,001
Cash and cash equivalents at end of period	\$53,278	\$8,519
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION		
Cash paid for interest, net of amounts capitalized	\$14,294	\$14,310
Cash paid for income taxes	1,517	2,329
Cash received from income tax refunds	13,281	5,650
SUPPLEMENTAL DISCLOSURES OF NON-CASH INVESTING AND FINANCING ACTIVITIES		
Changes in accrued property, plant and equipment	\$88,859	\$3,845
Non-cash additions to property, plant and equipment	—	4,525
The accompanying condensed notes are an integral part of these consolidated financial statements.		

Clearwater Paper Corporation
Condensed Notes to Consolidated Financial Statements
Unaudited

NOTE 1 Nature of Operations and Basis of Presentation

GENERAL

Clearwater Paper manufactures quality consumer tissue, away-from-home tissue, parent roll tissue, bleached paperboard and pulp at manufacturing facilities across the nation. The company is a premier supplier of private label tissue to major retailers and wholesale distributors, including grocery, drug, mass merchants and discount stores. In addition, the company produces bleached paperboard used by quality-conscious printers and packaging converters, and offers services that include custom sheeting, slitting and cutting. Clearwater Paper's employees build shareholder value by developing strong customer relationships through quality and service.

In the second half of 2017, we began a review of our selling, general and administrative cost structure as part of our effort to maintain our longer-term competitiveness. As a result of this review, in the fourth quarter of 2017 we began executing on a plan that is expected to result in lower selling, general and administrative expenses beginning in 2018. For the six months ended June 30, 2018, we incurred \$6.2 million of expenses associated with these efforts, which consisted primarily of severance and professional services expenses.

On March 31, 2017, we closed our Oklahoma City, Oklahoma facility. In the first half of 2017, we incurred \$6.0 million of costs associated with this closure, which included \$3.7 million in accelerated depreciation.

FINANCIAL STATEMENT PREPARATION AND PRESENTATION

The accompanying Consolidated Balance Sheets at June 30, 2018 and December 31, 2017, the related Consolidated Statements of Operations, and Comprehensive Income for the three and six months ended June 30, 2018 and 2017, and Condensed Consolidated Statements of Cash Flows for the six months ended June 30, 2018 and 2017, have been prepared in conformity with accounting principles generally accepted in the United States of America, or GAAP. We believe that all adjustments necessary for a fair presentation of the results of the interim periods presented have been included. The results of operations for any interim period are not necessarily indicative of the results of operations to be expected for the full year.

This Quarterly Report on Form 10-Q should be read in conjunction with our Annual Report on Form 10-K for the year ended December 31, 2017, as filed with the Securities and Exchange Commission, or SEC, on February 21, 2018.

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

SIGNIFICANT ESTIMATES

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of net sales and expenses during the reporting periods. Significant areas that may require the use of estimates and measurement of uncertainty include determination of net realizable value for deferred tax assets, uncertain tax positions, assessment of impairment of long-lived assets, variable consideration or reductions to revenue, revenue recognition estimates related to allocating the transaction price to various performance obligations, goodwill and intangibles, assessment of environmental matters, equity-based compensation and pension and postretirement obligation assumptions. Actual results could differ from those estimates and assumptions.

CASH AND CASH EQUIVALENTS

We consider all highly liquid instruments with maturities of three months or less at date of purchase to be cash equivalents.

PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment are stated at cost, including any interest costs capitalized, less accumulated depreciation. Depreciation of buildings, equipment and other depreciable assets is determined using the straight-line method. Assets we acquire through business combinations have estimated lives that are typically shorter than the assets we construct or buy new. Accumulated depreciation totaled \$1,678.6 million and \$1,636.3 million at June 30, 2018 and December 31, 2017, respectively.

For the six months ended June 30, 2018, we capitalized \$2.6 million of interest expense associated with the construction of a paper machine at our Shelby, North Carolina consumer products facility and \$0.6 million of interest expense associated with the construction of a continuous pulp digester at our Lewiston, Idaho pulp and paperboard facility. For the six months ended June 30, 2017, we capitalized \$1.8 million of interest expense associated with the continuous pulp digester project and \$0.2 million associated with the Shelby paper machine.

Consistent with authoritative guidance, we assess the carrying amount of long-lived assets with definite lives that are held-for-use and evaluate them for recoverability whenever events or changes in circumstances indicate that we may be unable to recover the carrying amount of the assets.

REVENUE RECOGNITION

We enter into contracts that can include various combinations of tissue and paperboard products, which are generally capable of being distinct and accounted for as separate performance obligations.

Revenue is recognized at a point in time upon transfer of control of promised products or services to customers in an amount that reflects the consideration we expect to receive in exchange for those products or services. Transfer of control typically occurs when the title and risk of loss passes to the customer. Shipping terms generally indicate when title and the risk of loss have passed. Revenue is recognized at shipment for sales when shipping terms are free on board, or FOB, shipping point. For sales where shipping terms are FOB destination, revenue is recognized when the goods are received by the customer. Revenue from both domestic and foreign sales of our products can involve shipping terms of either FOB shipping point or FOB destination or other shipping terms, depending upon the sales agreement with the customer. We have elected to treat shipping and handling costs for FOB shipping point contracts as a fulfillment cost, not as a separate performance obligation. No revenue is recognized over time. We typically expense incremental direct costs of obtaining a contract (sales commissions) when incurred because the amortization period is generally 12 months or less. We have also elected to use the practical expedient to not disclose unsatisfied or partially satisfied performance obligations as we have no unsatisfied contracts where the remaining portions are expected to be satisfied in a period greater than one year.

We provide for trade promotions, customer cash discounts, customer returns and other deductions as reductions to net sales, which are accounted for as variable consideration when estimating the amount of revenue to recognize. Returns and credits are estimated at contract inception and updated at the end of each reporting period as additional information becomes available. Revenue net of returns and credits is only recognized to the extent that it is probable that a significant reversal of any incremental revenue will not occur. Significant judgment is required to determine the most probable amount of variable consideration to apply as a reduction to net sales. Revenue is recognized net of any taxes collected from customers, which are subsequently remitted to governmental authorities.

Payment terms and conditions vary by contract type. Terms generally include a requirement of payment within 30 days, and do not include a significant financing component.

Trade accounts receivable are stated at the amount we expect to collect. Trade accounts receivable do not bear interest. The allowance for doubtful accounts is our best estimate of the losses we expect will result from the inability of our customers to make required payments. We generally determine the allowance based on a combination of actual historical write-off experience and an analysis of specific customer accounts. As of June 30, 2018 and December 31, 2017, we had allowances for doubtful accounts of \$1.3 million and \$1.4 million, respectively.

Refer to Note 15, "Segment Information," for further information, including the disaggregation of revenue by segment, primary geographical market, and major product type.

ACCOUNT PURCHASE AGREEMENT

In June 2018, we entered into an agreement (the “Account Purchase Agreement”) to offer to sell, on a revolving and discounted basis, certain trade accounts receivable balances to an unrelated third-party financial institution. If the financial institution purchases receivables thereunder, in its sole discretion, such transfers are accounted for as sales of receivables resulting in the receivables being de-recognized from our Consolidated Balance Sheet. The Account Purchase Agreement provides for the continuing sale of certain receivables on a revolving basis until June 2020 and automatically renews for successive one year terms, unless either

party elects to terminate the Account Purchase Agreement in accordance with its terms. The maximum amount of receivables that may be sold at any time, prior to the settlement thereof, is \$60.0 million.

For the quarter ended June 30, 2018, \$22.0 million of receivables had been sold under the Account Purchase Agreement. The proceeds from these sales of receivables are included within the change in receivables in the operating activities section of the Condensed Consolidated Statements of Cash Flows. The recorded factoring expense on sale of receivables is less than \$0.1 million for the quarter ended June 30, 2018 and is included in the "Selling, general and administrative expenses" line in the Consolidated Statement of Operations.

We have no retained interest in the receivables sold under the Account Purchase Agreement, however, we do have collection and administrative responsibilities for the sold receivables. The fair value of the servicing arrangement was not material to the financial statements.

STOCKHOLDERS' EQUITY

On December 15, 2015, we announced that our Board of Directors had approved a stock repurchase program authorizing the repurchase of up to \$100 million of our common stock. The repurchase program authorizes purchases of our common stock from time to time through open market purchases, negotiated transactions or other means, including accelerated stock repurchases and 10b5-1 trading plans in accordance with applicable securities laws and other restrictions. We have no obligation to repurchase stock under this program and may suspend or terminate the program at any time. In total, we have repurchased 1,440,696 shares of our outstanding common stock pursuant to this repurchase program, of which 84,750 shares were repurchased during the first half of 2017 at an average price of \$57.53 per share. We did not repurchase shares during the first half of 2018. As of June 30, 2018, we had up to \$29.8 million of authorization remaining pursuant to this stock repurchase program.

DERIVATIVES

We had no activity during the three and six months ended June 30, 2018 and 2017 that required hedge or derivative accounting treatment. To help mitigate our exposure to market risk for changes in utility commodity pricing, we use firm price contracts to supply a portion of the natural gas requirements for our manufacturing facilities. As of June 30, 2018, these contracts covered approximately 29% of our expected average monthly natural gas requirements for the remainder of 2018. Historically, these contracts have qualified for treatment as "normal purchases or normal sales" under authoritative guidance and thus required no mark-to-market adjustment.

NOTE 2 Recently Adopted and New Accounting Standards

Recently Adopted

In February 2018, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2018-02, Income Statement - Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income to allow for reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the Tax Cuts and Jobs Act (Act). This ASU also requires certain disclosures about stranded tax effects. We adopted this standard on January 1, 2018, which resulted in the reclassification of \$12.9 million between retained earnings and accumulated other comprehensive loss (AOCL), increasing retained earnings and AOCL within the equity section of our Consolidated Balance Sheet.

In May 2017, the FASB issued ASU 2017-09, Compensation—Stock Compensation (Topic 718): Scope of Modification Accounting to clarify when to account for a change to the terms or conditions of a share-based payment award as a modification. Under the new guidance, modification accounting is required only if the fair value, the vesting conditions, or the classification of the award (as equity or liability) changes as a result of the change in terms or conditions. The ASU was effective prospectively for annual periods beginning after December 15, 2017, including interim periods within those annual periods. We adopted this standard on January 1, 2018. The adoption of this ASU did not have a material impact on our consolidated financial statements.

In March 2017, the FASB issued ASU 2017-07, Compensation - Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost. The standard requires that an employer disaggregate the service cost component, presented within the "Cost of sales" and "Selling, general, and administrative" line items on our Consolidated Statements of Operations, from the other components of net periodic cost (benefit), which are now presented within the "Non-operating pension and other postretirement benefit (costs) income" line item in our Consolidated Statements of Operations. We adopted the standard effective January 1, 2018, which resulted in the retrospective presentation in the income statement of the disaggregated components and the prospective changes to the capitalized portion of both service cost and the other components within inventory. The adoption did not have a material impact on our consolidated financial statements. Refer to Note 10, "Pension and Other Postretirement Employee Benefit Plans," for further information, including the amounts associated with the reclassification of the components of net periodic cost as operating and non-operating.

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers (Topic 606). The core principle of the new standard is for companies to recognize revenue in a manner that depicts the transfer of goods or services to customers in amounts that reflect the consideration, or payment, to which the company expects to be entitled in exchange for those goods or services. The standard requires enhanced disclosures about revenue, including revenue recognition policies to identify performance obligations to customers and significant judgments in measurement and recognition. We adopted the new revenue guidance effective January 1, 2018 using the cumulative effect method, and did not have an adjustment to retained earnings upon adoption. The standard was applied to open contracts at the date of initial application. Aside from expanded disclosures, the adoption of Topic 606 did not have a material impact on our consolidated financial statement line items, processes, or internal controls. Refer to Note 1, "Nature of Operations and Basis of Presentation," for information about the basis of revenue recognition, and Note 15, "Segment Information," for further information including the disaggregation of revenue by segment, primary geographical market, and major product type.

New Accounting Standards

In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842). The new standard establishes a right-of-use (ROU) model that requires a lessee to record a ROU asset and a lease liability on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the income statement. The new standard is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. We expect the adoption of this ASU will increase both our assets and liabilities presented on our Consolidated Balance Sheets to reflect the ROU assets and corresponding lease liabilities, as well as increase our leasing disclosures. As of December 31, 2017, the total future minimum lease payments for our operating leases totaled \$75.3 million. We plan to adopt this standard on January 1, 2019. We are continuing our assessment and review of existing leases, implementing a leasing software solution, and

addressing necessary policy and process changes in preparation for adoption.

We reviewed all other new accounting pronouncements issued in the period and concluded that they are not applicable to our business.

NOTE 3 Inventories

Inventories at the balance sheet dates consist of:

(In thousands)	June 30, 2018	December 31, 2017
Pulp, paperboard and tissue products	\$163,426	\$ 165,281
Materials and supplies	87,369	85,987
Logs, pulpwood, chips and sawdust	11,418	14,775
	\$262,213	\$ 266,043

NOTE 4 Intangible Assets and Goodwill

Intangible assets at the balance sheet dates are comprised of the following:

(Dollars in thousands, lives in years)	June 30, 2018			
	Weighted Average Useful Life	Historical Cost	Accumulated Amortization	Net Balance
Customer relationships	9.3	\$ 62,401	\$ (37,409)	\$24,992
Trade names and trademarks	7.4	6,786	(3,514)	3,272
Other intangibles	6.0	572	(194)	378
		\$ 69,759	\$ (41,117)	\$28,642

(Dollars in thousands, lives in years)	December 31, 2017			
	Weighted Average Useful Life	Historical Cost	Accumulated Amortization	Net Balance
Customer relationships	9.3	\$ 62,401	\$ (34,061)	\$28,340
Trade names and trademarks	7.4	6,786	(3,000)	3,786
Non compete agreements	5.0	574	(574)	—
Other intangibles	6.0	572	(156)	416
		\$ 70,333	\$ (37,791)	\$32,542

For the three months ended June 30, 2018 and 2017, intangible assets amortization expense was \$2.0 million and \$2.1 million, respectively. For the six months ended June 30, 2018 and 2017, intangible assets amortization expense was \$3.9 million and \$4.0 million, respectively.

Goodwill is not amortized but is reviewed for impairment annually as of November 1 and at any time when events indicate impairment may have occurred. During the quarter ended June 30, 2018, we identified indicators of possible goodwill impairment for our Consumer Products reporting unit, namely the decline in actual results compared to the forecast used as part of our annual goodwill assessment performed in the fourth quarter of 2017, as well as a decline in our stock price. As a result, we performed a qualitative assessment and determined that it was more likely than not that the fair value of the reporting unit was greater than its carrying amount. Therefore, there was no impairment of goodwill as of June 30, 2018.

NOTE 5 Income Taxes

Consistent with authoritative guidance, our estimated annual effective tax rate is used to allocate expected annual income tax expense to interim periods. The rate is the ratio of estimated annual income tax expense to estimated pre-tax ordinary income, and excludes "discrete items," which are significant, unusual or infrequent items reported separately net of their related tax effect. The estimated annual effective tax rate is applied to the current interim period's ordinary income to determine the income tax expense allocated to the interim period. The income tax effects of discrete items are then determined separately and recognized in the interim period in which the income or expense items arise.

Our estimated annual effective tax rate applied to the second quarter of 2018 is approximately 26%, compared with approximately 33% for the comparable interim period in 2017. The decrease in the rate is primarily due to the rate reduction enacted with the Tax Cuts and Jobs Act.

NOTE 6 Accounts Payable and Accrued Liabilities

Accounts payable and accrued liabilities at the balance sheet dates consist of:

(In thousands)	June 30, 2018	December 31, 2017
Trade accounts payable	\$271,781	\$ 169,293
Accrued wages, salaries and employee benefits	37,485	41,979
Accrued interest	12,400	12,723
Accrued discounts and allowances	8,332	7,283
Accrued taxes other than income taxes payable	6,495	6,907
Accrued utilities	6,087	6,759
Other	15,008	11,677
	\$357,588	\$ 256,621

NOTE 7 Debt

REVOLVING CREDIT FACILITIES

As of June 30, 2018, there was an aggregate of \$160.0 million in borrowings outstanding under the credit facilities and \$7.6 million of the credit facilities was being used to support outstanding standby letters of credit. As of December 31, 2017, there was an aggregate of \$155.0 million in borrowings outstanding under the credit facilities. The borrowings outstanding under the revolving credit facilities as of June 30, 2018, consisted of short-term base and LIBOR rate loans and are classified as current liabilities in our Consolidated Balance Sheet. As of June 30, 2018, we would have been permitted to draw an additional \$132.4 million under the credit facilities.

NOTE 8 Other Long-Term Obligations

Other long-term obligations at the balance sheet dates consist of:

(In thousands)	June 30, 2018	December 31, 2017
Long-term lease obligations, net of current portion	\$25,778	\$ 26,460
Deferred proceeds	5,043	5,576
Deferred compensation	2,586	5,023
Other	4,327	6,216
	\$37,734	\$ 43,275

NOTE 9 Accumulated Other Comprehensive Loss

Accumulated other comprehensive loss, net of tax, is comprised of the following:

(In thousands)	Pension and Other Post Retirement Employee Benefit Plan Adjustments
Balance at December 31, 2016	\$ (51,753)
Other comprehensive income, net of tax ¹	527
Balance at June 30, 2017	\$ (51,226)
Balance at December 31, 2017	\$ (43,983)
Other comprehensive income, net of tax ¹	2,755
Reclassification of the income tax effects of the Tax Cuts and Jobs Act	(12,852)
Balance at June 30, 2018	\$ (54,080)

Included in other comprehensive income are net periodic costs associated with our pension and other postretirement employee benefit (OPEB) plans that were reclassified from accumulated other comprehensive loss. For the six months ended June 30, 2018 and 2017, actuarial loss amortization of \$3.4 million and \$1.0 million, respectively, as well as \$0.6 million and \$0.5 million, respectively, of prior service credit amortization were reclassified. These amounts are net of tax totaling \$1.0 million and \$0.3 million for each respective period. These accumulated other comprehensive loss components are included in the computation of net periodic pension and OPEB costs in Note 10, "Pension and Other Postretirement Employee Benefit Plans."

NOTE 10 Pension and Other Postretirement Employee Benefit Plans

The following table details the components of net periodic cost of our company-sponsored pension and OPEB plans for the periods presented:

(In thousands)	Three Months Ended June 30,			
	2018	2017	2018	2017
	Pension Benefit Plans		Other Postretirement Employee Benefit Plans	
Service cost	\$461	\$474	\$ 20	\$ 13
Interest cost	3,010	3,296	611	667
Expected return on plan assets	(4,247)	(4,688)	—	(1)
Amortization of prior service cost (credit)	—	2	(419)	(384)
Amortization of actuarial loss (gain)	2,458	2,412	(226)	(1,821)
Net periodic cost (benefit)	\$1,682	\$1,496	\$ (14)	\$ (1,526)

(In thousands)	Six Months Ended June 30,			
	2018	2017	2018	2017
	Pension Benefit Plans		Other Postretirement Employee Benefit Plans	
Service cost	\$895	\$1,034	\$ 68	\$ 81
Interest cost	6,010	6,574	1,218	1,371
Expected return on plan assets	(8,501)	(9,382)	—	(1)
Amortization of prior service cost (credit)	—	4	(838)	(767)
Amortization of actuarial loss (gain)	5,028	4,937	(451)	(3,301)

Edgar Filing: Clearwater Paper Corp - Form 10-Q

Net periodic cost (benefit) \$3,432 \$3,167 \$ (3) \$ (2,617)

During the six months ended June 30, 2018 and 2017, we made no contributions to our qualified pension plans. We do not expect, nor are we required, to make contributions in 2018.

During the six months ended June 30, 2018, we made contributions of \$0.2 million to our company-sponsored non-qualified pension plan. We estimate contributions will total \$0.4 million in 2018. We do not anticipate funding our OPEB plans in 2018 except to pay benefit costs as incurred during the year by plan participants.

On January 1, 2018 we adopted ASU 2017-07, which allows for only the service cost component of net periodic cost to be included as an operating cost. The other components of net periodic costs are to be included as non-operating costs in the accompanying Consolidated Statements of Operations. During the three and six months ended June 30, 2018, \$0.3 million and \$0.5 million of net periodic pension and OPEB service costs were charged to "Cost of sales," \$0.2 million and \$0.4 million were charged to "Selling, general and administrative expenses," and \$1.2 million and \$2.5 million were charged to "Non-operating pension and other post retirement benefit (costs) income" in the accompanying Consolidated Statements of Operations, respectively.

The adoption of ASU 2017-07 also required the reclassification of all prior period costs other than service costs from operating to non-operating. During the three and six months ended June 30, 2017, \$0.3 million and \$0.7 million of net periodic costs were charged to "Cost of sales," \$0.2 million and \$0.4 million were charged to "Selling, general and administrative expenses," and \$0.5 million and \$0.6 million of income was charged to "Non-operating pension and other postretirement benefit (costs) income" in the accompanying Consolidated Statements of Operations, respectively.

NOTE 11 Earnings per Common Share

Basic earnings per share are based on the weighted average number of shares of common stock outstanding. Diluted earnings per share are based upon the weighted average number of shares of common stock outstanding plus all potentially dilutive securities that were assumed to be converted into common shares at the beginning of the period under the treasury stock method.

The following table reconciles the number of common shares used in calculating the basic and diluted net earnings per share:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2018	2017	2018	2017
Basic weighted-average common shares outstanding ¹	16,486,064	15,196,196	16,491,364	17,052,525
Incremental shares due to:				
Restricted stock units	20,970	37,703	29,530	35,922
Performance shares	47,266	78,351	52,051	74,975
Stock options	—	16,868	90	30,636
Diluted weighted-average common shares outstanding	16,555,167	15,190,118	16,573,167	17,112,058
Basic net earnings per common share	\$0.42	\$ 0.49	\$0.58	\$ 0.94
Diluted net earnings per common share	0.42	0.48	0.58	0.94

Anti-dilutive shares excluded from calculation 1,029,985 1,322 912,864 93,150

¹ Basic average common shares outstanding include restricted stock awards that are fully vested, but are deferred for future issuance.

NOTE 12 Equity-Based Compensation

We recognize equity-based compensation expense for all equity-based payment awards made to employees and directors, including restricted stock units, or RSUs, performance shares and stock options, based on estimated fair values.

EMPLOYEE AWARDS

Employee equity-based compensation expense was recognized as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
(In thousands)	2018	2017	2018	2017
Restricted stock units	\$582	\$503	\$1,004	\$795
Performance shares	377	630	910	1,226
Stock options	593	736	1,128	1,315
Total employee equity-based compensation expense	\$1,552	\$1,869	\$3,042	\$3,336

Edgar Filing: Clearwater Paper Corp - Form 10-Q

As provided in the Clearwater Paper Corporation 2008 and 2017 Stock Incentive Plans, the following performance measures are used to determine the number of performance shares ultimately issuable:
For performance shares granted in 2017, the performance measure used for 40% of the grant is a comparison of the percentile ranking of our total stockholder return, or TSR, compared to the TSR of a selected index, and for 60% of the

13

performance share awards granted the performance measure used is a return on invested capital, or ROIC, performance measure.

For performance shares granted in 2018, the performance measure used for 40% of the performance share awards granted is an ROIC performance measure. For the remaining 60% of the grants, a free cash flow performance measure is used. The combined performance of these measures is then subject to an adjustment (increase or decrease) of up to 25% based on our TSR compared to the TSR performance of a selected index.

The number of performance shares actually issued, as a percentage of the amount subject to the performance share award, could range from 0%-200%.

During the first six months of 2018, 19,133 RSUs were settled and distributed. After adjusting for minimum tax withholdings, a net 13,221 shares were issued. In connection with the issued RSUs, the minimum tax withholding payments made during the six months ended June 30, 2018 totaled \$0.2 million.

During the six months ended June 30, 2018, we had 4,731 stock option awards expire with a weighted-average exercise price of \$64.31. At June 30, 2018, we had 300,021 stock option awards that were exercisable with a weighted-average exercise price of \$63.18.

The following table summarizes the number of share-based awards granted under the Clearwater Paper Corporation 2017 Stock Incentive Plan during the six months ended June 30, 2018 and the grant-date fair value of the awards:

	Six Months Ended June 30, 2018	
	Number of Shares Subject to Award	Average Fair Value of Award Per Share
Restricted stock units	108,816	\$ 37.45
Performance shares	49,040	37.45
Stock options	196,488	14.51

DIRECTOR AWARDS

Annually, each outside member of our Board of Directors receives deferred equity-based awards that are measured in units of our common stock and ultimately settled in cash at the time of payment. Accordingly, the compensation expense associated with these awards is subject to fluctuations each quarter based on mark-to-market adjustments at each reporting period in line with changes in the market price of our common stock. As a result of the mark-to-market adjustment, we recorded director equity-based compensation benefit of \$2.0 million and \$1.5 million for the three months ended June 30, 2018 and 2017, respectively. For the six months ended June 30, 2018 and 2017, we recorded director equity-based compensation benefit of \$2.7 million and \$2.9 million, respectively.

As of June 30, 2018, the liability amounts associated with director equity-based compensation included in "Other long-term obligations" and "Accounts payable and accrued liabilities" on the accompanying Consolidated Balance Sheet were \$0.8 million and \$1.2 million, respectively. At December 31, 2017, the liability amounts associated with director equity-based compensation included in "Other long-term obligations" and "Accounts payable and accrued liabilities" totaled \$3.6 million and \$2.4 million, respectively.

NOTE 13 Fair Value Measurements

The estimated fair values of our financial instruments at the dates presented below are as follows:

(In thousands)	June 30, 2018		December 31, 2017	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Cash and cash equivalents (Level 1)	\$53,278	\$53,278	\$15,738	\$15,738
Borrowings under revolving credit facilities (Level 2)	160,000	159,971	155,000	154,882
Long-term debt (Level 2)	575,000	525,625	575,000	569,250

Accounting guidance establishes a framework for measuring the fair value of financial instruments, providing a hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities, or "Level 1" measurements, followed by quoted prices of similar assets or observable market data considering the assets' underlying maturities, or "Level 2" measurements, and the lowest priority to unobservable inputs, or "Level 3" measurements.

The asset's or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used should seek to maximize the use of observable inputs and minimize the use of unobservable inputs.

Cash and cash equivalents, borrowings under the revolving credit facilities and long-term debt are the only items measured at fair value on a recurring basis.

We do not have any financial assets measured at fair value on a nonrecurring basis. Nonfinancial assets measured at fair value on a nonrecurring basis include items such as long-lived assets held and used that are measured at fair value resulting from impairment, if deemed necessary.

NOTE 14 Business Interruption and Insurance Recovery

In the first quarter of 2017, our financial statements included the impact of two separate fires, one of which occurred in the fourth quarter of 2016. Both claims were finalized in the first quarter of 2017 and the net proceeds from our insurance provider of \$4.3 million was included in "Cost of Sales" in our Consolidated Statement of Operations for the six months ended June 30, 2017.

There was no business interruption insurance activity in the six months ended June 30, 2018 at any of our facilities.

NOTE 15 Segment Information

Our reportable segments are described below.

Consumer Products

Our Consumer Products segment manufactures and sells a complete line of at-home tissue products, or retail products, and away-from-home tissue products, or non-retail products, and parent rolls. Retail products include bath, paper towels, facial and napkin product categories. Non-retail products include conventional one and two-ply bath tissue, two-ply paper towels, hard wound towels and dispenser napkins sold to customers with commercial and industrial tissue needs. Each category is further distinguished according to quality segments: ultra, premium, value and economy.

Pulp and Paperboard

Our Pulp and Paperboard segment manufactures and markets solid bleached sulfate paperboard for the high-end segment of the packaging industry as well as offers custom sheeting, slitting and cutting of paperboard. Our overall production consists primarily of folding carton, liquid packaging, cup and plate products and commercial printing grades. The majority of our Pulp and Paperboard customers are packaging converters, folding carton converters, merchants and commercial printers.

The table below presents information about our reportable segments:

(In thousands)	Three Months Ended		Six Months Ended	
	June 30, 2018	2017	June 30, 2018	2017
Segment net sales:				
Consumer Products	\$221,585	\$231,912	\$460,427	\$474,335
Pulp and Paperboard	210,514	197,751	408,624	392,853
Total segment net sales	\$432,099	\$429,663	\$869,051	\$867,188
Earnings (loss) before income taxes:				
Consumer Products ^{1,2,3}	\$(3,604)	\$10,698	\$(1,975)	\$16,902
Pulp and Paperboard ^{2,3}	34,192	21,071	60,346	48,271
Corporate ^{2,3}	(12,207)	(12,621)	(28,451)	(25,515)
Income from operations	18,381	19,148	29,920	39,658
Interest expense, net	(7,723)	(7,673)	(15,743)	(15,716)
Non-operating pension and other postretirement benefit (costs) income ²	(1,187)	517	(2,466)	565
Earnings before income taxes	\$9,471	\$11,992	\$11,711	\$24,507
Depreciation and amortization:				
Consumer Products ¹	\$14,220	\$16,292	\$28,517	\$34,534
Pulp and Paperboard	9,361	8,356	18,790	16,461
Corporate	1,596	1,407	3,037	2,617
Total depreciation and amortization	\$25,177	\$26,055	\$50,344	\$53,612

Operating income for the Consumer Products segment for the three and six months ended June 30, 2017 includes ¹ \$0.3 million and \$6.0 million, respectively, of costs associated with the closure of the Oklahoma City facility. These costs for the six months ended June 30, 2017 include \$3.7 million of accelerated depreciation.

² As a result of the adoption of ASU 2017-07, certain pension and OPEB (costs) income have been reclassified from operating to non-operating income. The service cost component of pension and OPEB costs remains within segment operating income. Refer to Note 2, "Recently Adopted and New Accounting Standards," and Note 10, "Pension and Other Postretirement Benefit Plans," for additional detail.

³ Income (loss) from operations for the Consumer Products, Pulp and Paperboard and Corporate segments for the three months ended June 30, 2018 include \$0.2 million, \$0.1 million, and \$0.8 million, respectively, of expenses associated with our selling, general, and administrative cost control measures. Income (loss) from operations for the Consumer Products, Pulp and Paperboard and Corporate segments for the six months ended June 30, 2018 include \$1.7 million, \$0.4 million and \$4.1 million, respectively, of expenses associated with our selling, general and administrative cost control measures.

For the six months ended June 30, 2018 and 2017, one customer, the Kroger Company, accounted for approximately 13.4% and 15.2%, respectively, of our total company net sales.

Net sales, classified by the major geographic areas in which our customers are located and by major products, were as follows:

(In thousands)	Three Months		Six Months Ended	
	Ended June 30,		June 30,	
	2018	2017	2018	2017
Primary geographical markets:				
United States	\$412,231	\$409,876	\$833,051	\$831,843
Other countries	19,868	19,787	36,000	35,345
Total net sales	\$432,099	\$429,663	\$869,051	\$867,188
Major products:				
Retail tissue	\$197,767	\$211,589	\$418,652	\$429,726
Paperboard	210,514	197,751	408,624	392,853
Non-retail tissue	23,765	19,966	40,724	43,959
Other	53	357	1,051	650
Total net sales	\$432,099	\$429,663	\$869,051	\$867,188

NOTE 16 Supplemental Guarantor Financial Information

All of our subsidiaries that are 100% directly or indirectly owned by Clearwater Paper, guarantee our \$275 million aggregate principal amount of 4.5% senior notes issued in January 2013 and due 2023, which we refer to as the 2013 Notes, on a full and unconditional, and joint and several basis. There are no significant restrictions on the ability of the guarantor subsidiaries to make distributions to Clearwater Paper, the issuer of the 2013 Notes. The following tables present the results of operations, financial position and cash flows of Clearwater Paper and its subsidiaries, the guarantor subsidiaries, and the eliminations necessary to arrive at the information for Clearwater Paper on a consolidated basis.

Clearwater Paper Corporation

Consolidating Statement of Operations and Comprehensive Income

Three Months Ended June 30, 2018

(In thousands)	Issuer	Guarantor Subsidiaries	Eliminations	Total
Net sales	\$433,826	\$ 54,313	\$ (56,040)	\$432,099
Cost and expenses:				
Cost of sales	(394,260)	(47,918)	55,024	(387,154)
Selling, general and administrative expenses	(21,226)	(5,338)	—	(26,564)
Total operating costs and expenses	(415,486)	(53,256)	55,024	(413,718)
Income from operations	18,340	1,057	(1,016)	18,381
Interest expense, net	(7,627)	(96)	—	(7,723)
Non-operating pension and other postretirement benefit costs	(1,187)	—	—	(1,187)
Earnings before income taxes	9,526	961	(1,016)	9,471
Income tax provision	(2,574)	(186)	250	(2,510)
Equity in income of subsidiary	775	—	(775)	—
Net earnings	\$7,727	\$ 775	\$ (1,541)	\$6,961
Other comprehensive income, net of tax	1,336	—	—	1,336
Comprehensive income	\$9,063	\$ 775	\$ (1,541)	\$8,297

Clearwater Paper Corporation

Consolidating Statement of Operations and Comprehensive Income

Six Months Ended June 30, 2018

(In thousands)	Issuer	Guarantor Subsidiaries	Eliminations	Total
Net sales	\$889,003	\$ 100,526	\$ (120,478)	\$869,051
Cost and expenses:				
Cost of sales	(807,217)	(88,278)	115,908	(779,587)
Selling, general and administrative expenses	(48,858)	(10,686)	—	(59,544)
Total operating costs and expenses	(856,075)	(98,964)	115,908	(839,131)
Income from operations	32,928	1,562	(4,570)	29,920
Interest expense, net	(15,556)	(187)	—	(15,743)
Non-operating pension and other postretirement benefit costs	(2,466)	—	—	(2,466)
Earnings before income taxes	14,906	1,375	(4,570)	11,711
Income tax provision	(2,956)	(199)	1,005	(2,150)
Equity in income of subsidiary	1,176	—	(1,176)	—
Net earnings	\$13,126	\$ 1,176	\$ (4,741)	\$9,561
Other comprehensive income, net of tax	2,755	—	—	2,755
Comprehensive income	\$15,881	\$ 1,176	\$ (4,741)	\$12,316

Edgar Filing: Clearwater Paper Corp - Form 10-Q

Clearwater Paper Corporation
Consolidating Statement of Operations and Comprehensive Income
Three Months Ended June 30, 2017

(In thousands)	Issuer	Guarantor Subsidiaries	Eliminations	Total
Net sales	\$419,540	\$ 63,956	\$ (53,833)	\$429,663
Cost and expenses:				
Cost of sales	(376,112)	(57,942)	52,993	(381,061)
Selling, general and administrative expenses	(23,411)	(6,043)	—	(29,454)
Total operating costs and expenses	(399,523)	(63,985)	52,993	(410,515)
Income (loss) from operations	20,017	(29)	(840)	19,148
Interest expense, net	(7,582)	(91)	—	(7,673)
Non-operating pension and other postretirement benefit income	517	—	—	517
Earnings (loss) before income taxes	12,952	(120)	(840)	11,992
Income tax provision	(4,224)	(52)	321	(3,955)
Equity in loss of subsidiary	(172)	—	172	—
Net earnings (loss)	\$8,556	\$ (172)	\$ (347)	\$8,037
Other comprehensive income, net of tax	126	—	—	126
Comprehensive income (loss)	\$8,682	\$ (172)	\$ (347)	\$8,163

Clearwater Paper Corporation
Consolidating Statement of Operations and Comprehensive Income
Six Months Ended June 30, 2017

(In thousands)	Issuer	Guarantor Subsidiaries	Eliminations	Total
Net sales	\$839,755	\$ 140,505	\$ (113,072)	\$867,188
Cost and expenses:				
Cost of sales	(750,593)	(127,680)	110,152	(768,121)
Selling, general and administrative expenses	(46,976)	(12,433)	—	(59,409)
Total operating costs and expenses	(797,569)	(140,113)	110,152	(827,530)
Income from operations	42,186	392	(2,920)	39,658
Interest expense, net	(15,574)	(142)	—	(15,716)
Non-operating pension and other postretirement benefit income	565	—	—	565
Earnings before income taxes	27,177	250	(2,920)	24,507
Income tax provision	(10,010)	(7)	1,062	(8,955)
Equity in income of subsidiary	243	—	(243)	—
Net earnings	\$17,410	\$ 243	\$ (2,101)	\$15,552
Other comprehensive income, net of tax	527	—	—	527
Comprehensive income	\$17,937	\$ 243	\$ (2,101)	\$16,079

Clearwater Paper Corporation
Consolidating Balance Sheet
At June 30, 2018

(In thousands)	Issuer	Guarantor Subsidiaries	Eliminations	Total
ASSETS				
Current assets:				
Cash and cash equivalents	\$ 53,278	\$ —	\$ —	\$ 53,278
Receivables, net	95,309	23,417	—	118,726
Taxes receivable	8,740	44	—	8,784
Inventories	221,994	44,789	(4,570)	262,213
Other current assets	7,877	255	—	8,132
Total current assets	387,198	68,505	(4,570)	451,133
Property, plant and equipment, net	1,063,183	108,185	—	1,171,368
Goodwill	244,161	—	—	244,161
Intangible assets, net	1,567	27,075	—	28,642
Intercompany (payable) receivable	(6,795)) 2,225	4,570	—
Investment in subsidiary	158,176	—	(158,176)	—
Other assets, net	23,114	3,391	(2,412)	24,093
TOTAL ASSETS	\$ 1,870,604	\$ 209,381	\$ (160,588)	\$ 1,919,397
LIABILITIES AND STOCKHOLDERS' EQUITY				
Current liabilities:				
Borrowings under revolving credit facilities	\$ 160,000	\$ —	\$ —	\$ 160,000
Accounts payable and accrued liabilities	333,307	24,281	—	357,588
Current liability for pensions and other postretirement employee benefits	7,631	—	—	7,631
Total current liabilities	500,938	24,281	—	525,219
Long-term debt	570,908	—	—	570,908
Liability for pensions and other postretirement employee benefits	69,504	—	—	69,504
Other long-term obligations	37,734	—	—	37,734
Accrued taxes	2,262	854	—	3,116
Deferred tax liabilities	98,689	26,070	(2,412)	122,347
TOTAL LIABILITIES	1,280,035	51,205	(2,412)	1,328,828
Stockholders' equity excluding accumulated other comprehensive loss	644,649	158,176	(158,176)	644,649
Accumulated other comprehensive loss, net of tax	(54,080)) —	—	(54,080)
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$ 1,870,604	\$ 209,381	\$ (160,588)	\$ 1,919,397

Clearwater Paper Corporation
Consolidating Balance Sheet
At December 31, 2017

(In thousands)	Issuer	Guarantor Subsidiaries	Eliminations	Total
ASSETS				
Current assets:				
Cash and cash equivalents	\$ 15,738	\$—	\$—	\$ 15,738
Receivables, net	125,001	17,064	—	142,065
Taxes receivable	20,242	40	—	20,282
Inventories	228,311	41,594	(3,862)	266,043
Other current assets	8,587	74	—	8,661
Total current assets	397,879	58,772	(3,862)	452,789
Property, plant and equipment, net	936,659	114,323	—	1,050,982
Goodwill	244,161	—	—	244,161
Intangible assets, net	2,089	30,453	—	32,542
Intercompany payable	(2,807)	(1,055)	3,862	—
Investment in subsidiary	157,000	—	(157,000)	—
Other assets, net	21,413	2,696	(2,331)	21,778
TOTAL ASSETS	\$ 1,756,394	\$ 205,189	\$ (159,331)	\$ 1,802,252
LIABILITIES AND STOCKHOLDERS' EQUITY				
Current liabilities:				
Borrowings under revolving credit facilities	\$ 155,000	\$—	\$—	\$ 155,000
Accounts payable and accrued liabilities	235,439	21,182	—	256,621
Current liability for pensions and other postretirement employee benefits	7,631	—	—	7,631
Total current liabilities	398,070	21,182	—	419,252
Long-term debt	570,524	—	—	570,524
Liability for pensions and other postretirement employee benefits	72,469	—	—	72,469
Other long-term obligations	43,275	—	—	43,275
Accrued taxes	1,928	842	—	2,770
Deferred tax liabilities	94,694	26,165	(2,331)	118,528
TOTAL LIABILITIES	1,180,960	48,189	(2,331)	1,226,818
Stockholders' equity excluding accumulated other comprehensive loss	619,417	157,000	(157,000)	619,417
Accumulated other comprehensive loss, net of tax	(43,983)	—	—	(43,983)
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$ 1,756,394	\$ 205,189	\$ (159,331)	\$ 1,802,252

Clearwater Paper Corporation
Consolidating Statement of Cash Flows
Six Months Ended June 30, 2018

(In thousands)	Issuer	Guarantor Subsidiaries	Eliminations	Total
CASH FLOWS FROM OPERATING ACTIVITIES				
Net earnings	\$ 13,126	\$ 1,176	\$ (4,741)	\$ 9,561
Adjustments to reconcile net earnings to net cash flows from operating activities:				
Depreciation and amortization	39,905	10,439	—	50,344
Deferred taxes	2,979	(330)	—	2,649
Employee benefit plans	326	—	—	326
Deferred issuance costs on debt	716	—	—	716
Other non-cash adjustments, net	431	(4)	—	427
Changes in working capital, net	41,660	(6,051)	708	36,317
Changes in taxes receivable, net	11,502	(4)	—	11,498
Other, net	(436)	(526)	—	(962)
Net cash flows from operating activities	110,209	4,700	(4,033)	110,876
CASH FLOWS FROM INVESTING ACTIVITIES				
Additions to property, plant and equipment	(77,257)	(1,343)	—	(78,600)
Other, net	793	14	—	807
Net cash flows from investing activities	(76,464)	(1,329)	—	(77,793)
CASH FLOWS FROM FINANCING ACTIVITIES				
Borrowings on revolving credit facilities	124,063	—	—	124,063
Repayments of borrowings on revolving credit facilities	(119,063)	—	—	(119,063)
Investment from (to) parent	(662)	(3,371)	4,033	—
Other, net	(543)	—	—	(543)
Net cash flows from financing activities	3,795	(3,371)	4,033	4,457
Increase in cash and cash equivalents	37,540	—	—	37,540
Cash and cash equivalents at beginning of period	15,738	—	—	15,738
Cash and cash equivalents at end of period	\$ 53,278	\$ —	\$ —	\$ 53,278

Clearwater Paper Corporation
Consolidating Statement of Cash Flows
Six Months Ended June 30, 2017

(In thousands)	Issuer	Guarantor Subsidiaries	Eliminations	Total
CASH FLOWS FROM OPERATING ACTIVITIES				
Net earnings	\$ 17,410	\$ 243	\$ (2,101)	\$ 15,552
Adjustments to reconcile net earnings to net cash flows from operating activities:				
Depreciation and amortization	37,335	16,277	—	53,612
Deferred taxes	7,183	708	—	7,891
Employee benefit plans	(2,183)	—	—	(2,183)
Deferred issuance costs on long term debt	598	—	—	598
Other non-cash adjustments, net	727	345	—	1,072
Changes in working capital, net	(29,619)	46,811	6,550	23,742
Changes in taxes receivable, net	9,710	6	(5,487)	4,229
Other, net	(373)	(541)	—	(914)
Net cash flows from operating activities	40,788	63,849	(1,038)	103,599
CASH FLOWS FROM INVESTING ACTIVITIES				
Additions to property, plant and equipment	(82,582)	(3,127)	—	(85,709)
Other, net	20	397	—	417
Net cash flows from investing activities	(82,562)	(2,730)	—	(85,292)
CASH FLOWS FROM FINANCING ACTIVITIES				
Purchase of treasury stock	(4,875)	—	—	(4,875)
Borrowings on revolving credit facilities	117,000	—	—	117,000
Repayments of borrowings on revolving credit facilities	(144,000)	—	—	(144,000)
Investment from (to) parent	63,496	(64,534)	1,038	—
Other, net	(914)	—	—	(914)
Net cash flows from financing activities	30,707	(64,534)	1,038	(32,789)
Decrease in cash and cash equivalents	(11,067)	(3,415)	—	(14,482)
Cash and cash equivalents at beginning of period	19,586	3,415	—	23,001
Cash and cash equivalents at end of period	\$ 8,519	\$ —	\$ —	\$ 8,519

ITEM 2.
Management's
Discussion
and Analysis
of Financial
Condition
and Results
of Operations

FORWARD-LOOKING STATEMENTS

Our disclosure, discussion and analysis in this report contains, in addition to historical information, certain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, including statements regarding the costs, timing and benefits of optimization, cost management and strategic capital projects; costs, timing and benefits associated with the Shelby, North Carolina facility expansion; selling, general and administrative cost reduction initiative and savings; sales volume; operating costs, including transportation and purchased pulp; raw materials and input usage and costs; timing and costs related to major maintenance and repairs; capital expenditures; energy costs and usage; tax rates; cash flows; liquidity; credit agreement financial covenants; and market risks. Words such as anticipate, expect, intend, plan, target, project, believe, schedule, estimate, may, and similar expressions are intended to identify such forward-looking statements. These forward-looking statements are based on management's current expectations, estimates, assumptions and projections that are subject to change. Our actual results of operations may differ materially from those expressed or implied by the forward-looking statements contained in this report. Important factors that could cause or contribute to such differences include those risks discussed in the section entitled "Risk Factors" in our 2017 Form 10-K, as well as the following:

- competitive pricing pressures for our products, including as a result of increased capacity as additional manufacturing facilities are operated by our competitors;
- the loss of, changes in prices in regards to, or reduction in orders from a significant customer;
- changes in customer product preferences and competitors' product offerings;
- our ability to successfully implement our operational efficiencies and cost savings strategies, including related capital projects, and achieve the expected operational or financial results of those projects, including from the continuous digester at our Lewiston facility;
- our ability to execute on our expansion strategies, including on-time completion of our new tissue manufacturing operations in Shelby, North Carolina;
- customer acceptance and timing and quantity of purchases of our tissue products, including the existence of sufficient demand for and the quality of tissue produced by our expanded Shelby, North Carolina operations when completed;
- changes in the U.S. and international economies and in general economic conditions in the regions and industries in which we operate;
- labor disruptions;
- changes in transportation costs and disruptions in transportation services;
- changes in the cost and availability of wood fiber and wood pulp;
- manufacturing or operating disruptions, including IT system and IT system implementation failures, equipment malfunction and damage to our manufacturing facilities;
- changes in costs for and availability of packaging supplies, chemicals, energy and maintenance and repairs;
- cyclical industry conditions;
- changes in expenses and required contributions associated with our pension plans;
- environmental liabilities or expenditures;
- cyber-security risks;
- reliance on a limited number of third-party suppliers for raw materials;
- our ability to service our debt obligations;
- restrictions on our business from debt covenants and terms; and

•changes in laws, regulations or industry standards affecting our business.

Forward-looking statements contained in this report present management's views only as of the date of this report. Except as required under applicable law, we do not intend to issue updates concerning any future revisions of management's views to reflect events or circumstances occurring after the date of this report.

OVERVIEW

Background

We manufacture quality consumer tissue, away-from-home tissue, parent roll tissue, bleached paperboard and pulp at manufacturing facilities across the nation. We are a premier supplier of private label tissue to major retailers and wholesale distributors, including grocery, drug, mass merchant and discount stores. In addition, we produce bleached paperboard used by quality-conscious printers and packaging converters. Our employees build shareholder value by developing strong customer partnerships through quality and service.

Recent Events

Shelby Expansion Project

We are in the process of building a new tissue machine and related converting equipment at a site adjacent to our existing facility in Shelby, North Carolina. The new tissue machine will produce a variety of high-quality private label premium and ultra-premium bath, paper towel and napkin products. At full production capacity, the new tissue machine is expected to produce approximately 70,000 tons of tissue products annually. The estimated cost for the project includes approximately \$280 million for the tissue machine, converting equipment and buildings, and approximately \$60 million for the purchase and expansion of an existing warehouse that will consolidate all southeastern warehousing in Shelby. We project that the construction of the new facility will be completed in early 2019 and will be fully operational in 2020. During the six months ended June 30, 2018, we incurred costs of \$146.1 million on construction related activities and the new tissue machine in Shelby. We also capitalized \$2.6 million of interest in the first half of 2018 related to the Shelby expansion.

Selling, General and Administrative Cost Structure Changes

In the second half of 2017, we began a review of our selling, general and administrative, or SG&A, cost structure as part of our effort to maintain our longer-term competitiveness. As a result of this review, in the fourth quarter of 2017 we began executing on a plan that is expected to result in lower selling, general and administrative expenses beginning in 2018, and then is expected to result in at least \$20 million in annual SG&A savings beginning in 2019. For the six months ended June 30, 2018, we incurred \$6.2 million of expenses associated with these efforts, of which \$1.1 million was incurred in the second quarter and consisted primarily of severance and professional services expenses.

Components and Trends in our Business

Net sales

Net sales predominantly consist of sales of consumer tissue and paperboard products, net of discounts, returns and allowances and any sales taxes collected. Prices for our consumer tissue products tend to be primarily driven by competitive market conditions and the relative prices of branded tissue products. Demand and pricing for our pulp and paperboard products are largely determined by general global market conditions and the demand for high quality paperboard.

In recent years, the tissue industry has seen an increase in ultra tissue products as industry participants have added or improved through-air-dried, or TAD, or equivalent production capacity. Demand and pricing for consumer tissue products is currently being affected by increased supply as a result of new tissue machines that have been added or publicly announced in North America, as well as changing dynamics in the at-home tissue segment as a result of changing consumer purchasing habits, consolidations and new entrants in the consumer retail channel, and new and evolving sales and distribution channels. These changing conditions contribute to a very competitive environment for consumer tissue. In addition, in the third quarter of 2017, our largest tissue customer made the decision to go from a single source model to a multi-source model for their private label tissue supply beginning in the first quarter of 2018. This decision has primarily affected conventional tissue supply to this customer and we do not expect to be able to fully replace this lost volume in 2018 through sales to other customers, which resulted in reduced tissue sales in the second quarter of 2018 and is expected to result in a reduction in our overall tissue sales volume in 2018.

Our pulp and paperboard business is affected by macro-economic conditions around the world and has historically experienced cyclical market conditions. As a result, historical prices for our products and sales volumes have been

volatile. Product pricing is significantly affected by the relationship between supply and demand for our products. Product supply in the industry is influenced primarily by fluctuations in available manufacturing production, which tends to increase during periods when prices remain strong. In addition, currency exchange rates affect U.S. supplies of paperboard, as non-U.S. manufacturers are more attracted to the U.S. market when the dollar is relatively strong.

Cost of sales

(Dollars in thousands)	Three Months Ended June 30,					
	2018		2017			
	Cost	Percentage of Sales	Cost	Percentage of Sales	Cost	Variance
Wages and benefits	\$72,721	16.8 %	\$68,084	15.9 %		\$4,637
Transportation ¹	56,061	13.0	49,550	11.5		6,511
Purchased pulp	45,013	10.4	45,366	10.6		(353)
Chemicals	44,949	10.4	41,918	9.8		3,031
Chips, sawdust and logs	43,940	10.2	34,854	8.1		9,086
Packaging supplies	21,212	4.9	21,412	5.0		(200)
Depreciation	21,574	5.0	22,517	5.2		(943)
Energy	19,168	4.4	20,813	4.8		(1,645)
Maintenance and repairs ²	16,807	3.9	26,291	6.1		(9,484)
	341,445	79.0	330,805	77.0		10,640
Other operating costs	45,709	10.6	50,256	11.7		(4,547)
Total cost of sales	\$387,154	89.6 %	\$381,061	88.7 %		\$6,093

(Dollars in thousands)	Six Months Ended June 30,					
	2018		2017			
	Cost	Percentage of Sales	Cost	Percentage of Sales	Cost	Variance
Wages and benefits	\$143,173	16.5 %	\$141,531	16.4 %		\$1,642
Transportation ¹	110,867	12.8	96,403	11.1		14,464
Purchased pulp	93,267	10.7	91,458	10.5		1,809
Chemicals	87,623	10.0	82,639	9.5		4,984
Chips, sawdust and logs	82,367	9.5	70,086	8.1		12,281
Packaging supplies	44,204	5.1	43,890	5.1		314
Depreciation	43,296	5.0	46,907	5.4		(3,611)
Energy	40,026	4.6	44,302	5.1		(4,276)
Maintenance and repairs ²	35,457	4.1	45,166	5.2		(9,709)
	680,280	78.3	662,382	76.4		17,898
Other operating costs	99,307	11.4	105,739	12.2		(6,432)
Total cost of sales	\$779,587	89.7 %	\$768,121	88.6 %		\$11,466

Certain prior period amounts have been reclassified to conform with the current period presentation.

¹ Includes internal and external transportation costs.

² Excludes related internal labor costs.

Wages and benefits. Costs related to our employees primarily consist of wages and related benefit costs and payroll taxes. For the three and six months ended June 30, 2018, wage and benefit costs increased compared to the same periods in 2017, primarily due to severance related costs associated with our SG&A cost structure changes and the impact of annual wage increases, in addition to costs for hiring and training new employees for the Shelby expansion project.

Transportation. Fuel prices, mileage driven and line-haul rates largely impact transportation costs for the delivery of raw materials to our manufacturing facilities, internal inventory transfers and the delivery of our finished products to customers. Changing fuel prices particularly affect our margins for consumer products because we supply customers throughout the U.S. and transport unconverted parent rolls from our tissue mills to our tissue converting facilities. For the three and six months ended June 30, 2018, transportation costs increased compared to the same periods in 2017

primarily due to increased line haul rates and fuel prices, carrier availability and higher costs to service customer mix. We expect our transportation costs to be \$14 million to \$16 million higher in 2018 compared to 2017.

Purchased pulp. We purchase a significant amount of the pulp needed to manufacture our consumer products, and to a lesser extent our paperboard, from external suppliers. For the three months ended June 30, 2018, purchased pulp costs remained essentially flat compared to the same period in 2017. For the six months ended June 30, 2018, purchased pulp costs increased due to higher pricing. We expect our pulp and wood fiber costs to be \$15 million to \$17 million higher in 2018 compared to 2017.

Chemicals. We consume a substantial amount of chemicals in the production of pulp and paperboard, as well as in the production of through-air-dried, or TAD, tissue. The chemicals we generally use include polyethylene, caustic, starch, sodium chlorate, latex and paper processing chemicals. A portion of the chemicals used in our manufacturing processes, particularly in the paperboard extrusion process, are petroleum based and are impacted by petroleum prices. Chemical costs increased in the three and six months ended June 30, 2018, compared to the same periods in 2017, due to increased paperboard production and higher pricing for polyethylene, latex and caustic.

Chips, sawdust and logs. We purchase chips, sawdust and logs to manufacture pulp. We source residual wood fibers under both long-term and short-term supply agreements, as well as in the spot market. Chips, sawdust and log costs increased for the three and six months ended June 30, 2018, compared to the same periods in 2017, primarily due to increased paperboard production and higher prices for these materials at both of our pulp and paperboard locations.

Packaging supplies. As a significant producer of private label consumer tissue products, we package to order for retail chains, wholesalers and cooperative buying organizations. Under our agreements with those customers, we are responsible for the expenses related to the unique packaging of our products for direct retail sale to their consumers.

Packaging costs remained flat for the three and six months ended June 30, 2018, compared to the same periods in 2017, as higher pricing for packaging materials was offset by reduced shipments in our consumer products segment.

Depreciation. We record substantially all of our depreciation expense associated with our plant and equipment in "Cost of sales" on our Consolidated Statements of Operations. Depreciation expense for the three and six months ended June 30, 2018 decreased compared to the same period in 2017 primarily due to accelerating depreciation in 2017 on certain Oklahoma City assets in connection with the March 2017 facility closure, partially offset by increased depreciation as a result of higher capital spending.

Energy. We use energy in the form of electricity, hog fuel, steam and natural gas to operate our mills. Energy prices may fluctuate widely from period-to-period primarily due to volatility in temperatures and electricity and natural gas rates. We generally strive to reduce our exposure to volatile energy prices through conservation. In addition, a co-generation facility that produces steam and electricity at our Lewiston, Idaho manufacturing site helps to lower our energy costs. Energy costs for the three and six months ended June 30, 2018, decreased compared to the same periods in 2017, primarily due to favorable natural gas and electricity prices in our pulp and paperboard segment, in addition to lower natural gas usage at our Idaho pulp and paperboard facility.

To help mitigate our exposure to changes in natural gas prices, we use firm-price contracts to supply a portion of our natural gas requirements. As of June 30, 2018, these contracts covered approximately 29% of our expected average monthly natural gas requirements for the remainder of 2018.

Maintenance and repairs. We regularly incur significant costs to maintain our manufacturing equipment. We perform routine maintenance on our machines and periodically replace a variety of parts such as motors, pumps, pipes and electrical parts. Major equipment maintenance and repairs in our Pulp and Paperboard segment also require maintenance shutdowns approximately every 18 to 24 months at both our Idaho and Arkansas facilities, which increase costs and may reduce net sales in the quarters in which the major maintenance shutdowns occur. During the three and six months ended June 30, 2018, maintenance and repair spending was lower than the same periods in 2017 due to no planned major maintenance in our pulp and paperboard segment in the first half of 2018, in addition to lower planned maintenance in the second quarter of 2018.

Other. Other costs primarily consist of miscellaneous operating costs, which decreased in the three and six months ended June 30, 2018, compared to the same periods in 2017, primarily due to reduced purchased paper costs, professional service fees and operating supplies expense.

Selling, general and administrative expenses

Selling, general and administrative expenses primarily consist of compensation and associated expenses for sales and administrative personnel, as well as commission expenses related to sales of our products.

Interest expense

Interest expense for the three and six months ended June 30, 2018 and 2017 includes interest on our \$275 million aggregate principal amount of 4.5% senior notes issued in January 2013 and due 2023, which we refer to as the 2013 Notes, and interest on our \$300 million aggregate principal amount of 5.375% senior notes issued in 2014 and due 2025, which we refer to as the 2014 Notes. Interest expense also includes interest on the amount drawn under our revolving credit facilities and amortization of deferred issuance costs associated with all of our notes and revolving credit facilities.

Income taxes

Income taxes are based on reported earnings and tax rates in the jurisdictions in which our operations occur and offices are located, adjusted for available credits, changes in valuation allowances and differences between reported earnings and taxable income using current tax laws and rates. We generally expect our effective income tax rate, excluding discrete items, to remain fairly constant, although it could fluctuate due to changes in tax law.

RESULTS OF OPERATIONS

Three Months Ended June 30, 2018 Compared to Three Months Ended June 30, 2017

The following table sets forth data included in our Consolidated Statements of Operations as a percentage of net sales.

(Dollars in thousands)	Three Months Ended June 30,			
	2018		2017	
Net sales	\$432,099	100.0%	\$429,663	100.0%
Costs and expenses:				
Cost of sales	(387,154)	89.6	(381,061)	88.7
Selling, general and administrative expenses	(26,564)	6.1	(29,454)	6.9
Total operating costs and expenses	(413,718)	95.7	(410,515)	95.5
Income from operations	18,381	4.3	19,148	4.5
Interest expense, net	(7,723)	1.8	(7,673)	1.8
Non-operating pension and other postretirement benefit (costs) income	(1,187)	0.3	517	0.1
Earnings before income taxes	9,471	2.2	11,992	2.8
Income tax provision	(2,510)	0.6	(3,955)	0.9
Net earnings	\$6,961	1.6 %	\$8,037	1.9 %

Net sales—Second quarter 2018 net sales increased by \$2.4 million compared to the second quarter of 2017. This increase was primarily the result of increased paperboard sales volumes and prices, partially offset by reduced Consumer Products volumes and unfavorable product mix shifts in both segments. These items are further discussed below under “Discussion of Business Segments.”

Cost of sales—Cost of sales was 89.6% of net sales for the second quarter of 2018 and 88.7% of net sales for the same period in 2017. Our overall cost of sales were \$6.1 million higher than the second quarter of 2017, primarily due to higher input costs for transportation, chips, sawdust and logs, chemicals and wages and benefits. These higher costs were partially offset by lower maintenance, energy and internally sourced paperboard costs.

Selling, general and administrative expenses—Selling, general and administrative expenses for the second quarter of 2018 decreased \$2.9 million compared to the second quarter of 2017. The lower expense was primarily a result of lower expense associated with profit dependent accruals, as well as \$2.0 million of mark-to-market benefit during the second quarter of 2018, compared to \$1.5 million during the second quarter of 2017, related to our directors' common stock units, which will ultimately be settled in cash.

Interest expense—Interest expense for the second quarter of 2018 remained flat compared to the first quarter of 2017, as higher interest expense associated with a larger average balance on our revolving credit facilities was offset by higher capitalized interest in the second quarter of 2018.

Income tax provision—We recorded an income tax provision of \$2.5 million for the three months ended June 30, 2018, compared to \$4.0 million in the same period in 2017. The rate determined under generally accepted accounting principles, or GAAP, for the three months ended June 30, 2018 was approximately 27% compared to approximately 33% for the same period of 2017. The decrease to the rate was primarily the result of the federal rate reduction enacted with the Tax Cuts and Jobs Act.

During the second quarters of 2018 and 2017, there were a number of items that were included in the calculation of our income tax provision that we do not believe were indicative of our core operating performance. Excluding these items, the tax rate for the three months ended June 30, 2018 would have been approximately 27% compared to an adjusted rate of approximately 33% for the three months ended June 30, 2017. See the section entitled “Non-GAAP Measures” on page 32 of this report for a reconciliation of these adjusted income tax provision amounts to the comparable GAAP income tax provision amounts.

Discussion of Business Segments

28

Consumer Products

	Three Months Ended	
	June 30,	
(Dollars in thousands - except per ton amounts)	2018	2017
Net sales	\$221,585	\$231,912
Operating (loss) income	(3,604)	10,698
Percent of net sales	(1.6)%	4.6 %

Shipments (short tons)

Retail	73,070	77,714
Non-retail	17,316	13,736
Total tissue tons	90,386	91,450
Converted products cases (in thousands)	12,027	12,709

Sales price (per short ton)

Retail	\$2,707	\$2,723
Non-retail	1,372	1,454
Total tissue	\$2,451	\$2,533

Net sales for the Consumer Products segment during the second quarter of 2018 decreased by \$10.3 million compared to the second quarter of 2017 due to a reduction in sales volume, in addition to decreased pricing for some products and an unfavorable mix shift to increased parent roll sales. These decreases were partially offset by higher TAD towel, facial and bath sales.

The segment had an operating loss of \$3.6 million for the second quarter of 2018, compared to operating income of \$10.7 million in the second quarter of 2017 primarily due to the decreased sales, as well as higher costs in the second quarter of 2018 for transportation, maintenance and energy, and higher wages and benefits expense associated primarily with our selling, general and administrative cost reduction efforts. These unfavorable variances were partially offset by lower depreciation expense and reduced packaging and operating supplies costs.

Pulp and Paperboard

	Three Months Ended	
	June 30,	
(Dollars in thousands - except per ton amounts)	2018	2017
Net sales	\$210,514	\$197,751
Operating income	34,192	21,071
Percent of net sales	16.2 %	10.7 %

Paperboard shipments (short tons)	216,582	207,152
-----------------------------------	---------	---------

Paperboard sales price (per short ton)	\$972	\$955
--	-------	-------

Net sales for the Pulp and Paperboard segment increased by \$12.8 million during the second quarter of 2018, compared to the second quarter of 2017. The increase was due primarily to strong production and sales volume increases in addition to paperboard net price increases. This was slightly offset by an unfavorable mix shift from coated cup and liquid packaging to increased plate sales.

Operating income for the segment increased by \$13.1 million during the second quarter of 2018, compared to the second quarter of 2017, primarily due to reduced energy costs and planned major maintenance costs incurred in the second quarter 2017 that were not incurred in the second quarter of 2018. These favorable impacts were partially offset by higher chips, sawdust and log costs, as well as higher transportation, chemical and depreciation costs.

RESULTS OF OPERATIONS

Six Months Ended June 30, 2018 Compared to Six Months Ended June 30, 2017

The following table sets forth data included in our Consolidated Statements of Operations as a percentage of net sales.

(Dollars in thousands)	Six Months Ended June 30,			
	2018		2017	
Net sales	\$869,051	100.0%	\$867,188	100.0 %
Costs and expenses:				
Cost of sales	(779,587)	89.7	(768,121)	88.6
Selling, general and administrative expenses	(59,544)	6.9	(59,409)	6.9
Total operating costs and expenses	(839,131)	96.6	(827,530)	95.4
Income from operations	29,920	3.4	39,658	4.6
Interest expense, net	(15,743)	1.8	(15,716)	1.8
Non-operating pension and other postretirement benefit (costs) income	(2,466)	0.3	565	(0.1)
Earnings before income taxes	11,711	1.3	24,507	2.8
Income tax provision	(2,150)	0.2	(8,955)	1.0
Net earnings	\$9,561	1.1	\$15,552	1.8

Net sales—Net sales for the six months ended June 30, 2018 increased by \$1.9 million, or 0.2%, compared to the same period in 2017. The increase was primarily due to favorable prices and sales volume in our Pulp and Paperboard segment, offset by net price decreases and reduced shipment volumes in our Consumer Products segment. These items are further discussed below under “Discussion of Business Segments.”

Cost of sales—Cost of sales was 89.7% of net sales for the six months ended June 30, 2018 compared to 88.6% of net sales for the same period in 2017. Our overall costs of sales were \$11.5 million higher than the first six months of 2017 primarily due to increased transportation costs driven by higher line haul rates and fuel prices, carrier availability and higher costs to service customer mix, in addition to increased costs for wood fiber, chemicals and wages and benefits. These cost increases were partially offset by lower maintenance, energy and depreciation costs.

Selling, general and administrative expenses—Selling, general and administrative expenses for the six months ended June 30, 2018 were comparable with the same period in 2017. Expenses related to the selling, general, and administrative cost structure changes, which consisted primarily of severance and professional services expenses, were offset by lower profit dependent accruals, reduced commission expense and lower travel expenses.

Interest expense—Interest expense for the six months ended June 30, 2018 remained flat compared to the same period in 2017, as higher interest expense associated with a larger average balance on our revolving credit facilities was offset by higher capitalized interest in the 2018 period.

Income tax provision—We recorded an income tax provision of \$2.2 million in the six months ended June 30, 2018, compared to \$9.0 million in the same period of 2017. The rate determined under GAAP for the six months ended June 30, 2018 was approximately 18% compared to 37% for the same period of 2017. The net change to our effective tax rate in the six months ended June 30, 2017 was primarily the result of the federal rate reduction enacted with the Tax Cuts and Jobs Act.

During the six months ended June 30, 2018 and 2017, there were a number of items that were included in the calculation of our income tax provision that we do not believe were indicative of our core operating performance. Excluding these items, the tax rate for the six months ended June 30, 2018 would have been approximately 24% compared to an adjusted rate of approximately 36% for the six months ended June 30, 2017. See the section entitled “Non-GAAP Measures” on page 32 of this report for a reconciliation of these adjusted income tax provision amounts to the comparable GAAP income tax provision amounts.

Discussion of Business Segments

Consumer Products

(Dollars in thousands - except per ton amounts)	Six Months Ended	
	June 30,	
	2018	2017
Net sales	\$460,427	\$474,335
Operating (loss) income	(1,975)	16,902
Percent of net sales	(0.4)%	3.6 %

Shipments (short tons)

Retail	154,041	156,400
Non-retail	28,552	30,414
Total tissue tons	182,593	186,814
Converted products cases (in thousands)	25,289	25,832

Sales price (per short ton)

Retail	\$2,711	\$2,748
Non-retail	1,426	1,446
Total tissue	\$2,510	\$2,536

Net sales for our Consumer Products segment decreased \$13.9 million for the six months ended June 30, 2018, compared to the same period of 2017, due to lower average selling prices and decreased overall sales volumes in both retail and away from home cases. These unfavorable impacts were partially offset by a favorable sales mix driven by increased TAD bathroom tissue and paper towel sales combined with reduced parent roll sales.

The segment had an operating loss of \$2.0 million for the six months ended June 30, 2018, compared to operating income of \$16.9 million for the same period of 2017, largely due to the decreased sales volumes in addition to increased transportation costs, increased pulp pricing and higher expenses associated with our SG&A cost reduction efforts. These cost increases were partially offset by lower depreciation expense in the first half of 2018 due to accelerated depreciation in the first half of 2017 associated with the closure of our Oklahoma City facility, as well as lower packaging supplies and chemical costs.

Pulp and Paperboard

(Dollars in thousands - except per ton amounts)	Six Months Ended	
	June 30,	
	2018	2017
Net sales	\$408,624	\$392,853
Operating income	60,346	48,271
Percent of net sales	14.8 %	12.3 %

Paperboard shipments (short tons)	422,891	417,534
Paperboard sales price (per short ton)	\$966	\$941

Net sales for the Pulp and Paperboard segment increased by \$15.8 million during the six months ended June 30, 2018, compared to the same period of 2017. The increase was primarily due to price increases in addition to increased sales volume.

Operating income for the segment increased \$12.1 million during the six months ended June 30, 2018, compared to the same period of 2017, primarily due to increased sales, reduced maintenance costs due to no planned major maintenance in the first six months of 2018, and lower energy costs. These favorable impacts were partially offset by increased chips, sawdust and log costs, higher chemical and transportation costs, and higher depreciation expense.

NON-GAAP MEASURES

We use earnings before interest, taxes, depreciation and amortization, or EBITDA, EBITDA adjusted for certain items, or Adjusted EBITDA, and Adjusted income tax provision as supplemental performance measures that are not required by, or presented in accordance with GAAP. EBITDA and Adjusted EBITDA should not be considered as alternatives to net earnings, operating income or any other performance measure derived in accordance with GAAP, or as alternatives to cash flows from operating activities or a measure of our liquidity or profitability. In addition, our calculation of EBITDA and Adjusted EBITDA may or may not be comparable to similarly titled measures used by other companies.

We present EBITDA, Adjusted EBITDA and Adjusted income tax provision because we believe they assist investors and analysts in comparing our performance across reporting periods on a consistent basis by excluding items that we do not believe are indicative of our core operating performance. In addition, we use EBITDA and Adjusted EBITDA: (i) as factors in evaluating management's performance when determining incentive compensation, (ii) to evaluate the effectiveness of our business strategies and (iii) because our credit agreement and the indenture governing the 2013 Notes use metrics similar to EBITDA to measure our compliance with certain covenants.

The following table provides our EBITDA and Adjusted EBITDA for the periods presented, as well as a reconciliation to net earnings.

(In thousands)	Three Months Ended		Six Months Ended	
	June 30, 2018	2017	June 30, 2018	2017
Net earnings	\$6,961	\$8,037	\$9,561	\$15,552
Interest expense, net	7,723	7,673	15,743	15,716
Income tax provision	2,510	3,955	2,150	8,955
Depreciation and amortization expense ¹	25,177	26,055	50,344	53,612
EBITDA	\$42,371	\$45,720	\$77,798	\$93,835
Directors' equity-based compensation benefit	(1,990)	(1,483)	(2,699)	(2,933)
Reorganization related expenses associated with SG&A cost control measures	1,076	—	6,180	—
Consumer products reorganization related expenses	792	—	792	—
Other	338	—	338	—
Costs associated with Oklahoma City facility closure	—	275	—	2,349
Costs associated with Long Island facility closure	—	365	—	831
Manchester Industries acquisition related expenses	—	105	—	220
Write-off of assets as a result of Warehouse Automation project	—	41	—	41
Adjusted EBITDA	\$42,587	\$45,023	\$82,409	\$94,343

¹ Depreciation and amortization expense for the six months ended June 30, 2017 includes \$3.7 million of accelerated depreciation associated with the closure of our Oklahoma City facility.

The following table provides our Adjusted income tax provisions for the three and six months ended June 30, 2018 and 2017, as well as a reconciliation to the GAAP income tax benefit (provision).

(In thousands)	Three Months Ended		Six Months Ended	
	June 30, 2018	2017	June 30, 2018	2017
GAAP Income tax provision	\$(2,510)	\$(3,955)	\$(2,150)	\$(8,955)
Special items, tax impact:				
Directors' equity-based compensation benefit	518	495	695	988
Reorganization related expenses associated with SG&A cost control measures	(280)	—	(1,556)	—
Consumer products reorganization related expenses	(206)	—	(206)	—
Other	(88)	—	(88)	—
Impact of state tax rate changes	—	—	(676)	—
Costs associated with Oklahoma City facility closure	—	(92)	—	(2,043)
Manchester Industries acquisition related expenses	—	(35)	—	(74)
Costs associated with Long Island facility closure	—	(221)	—	(379)
Write off of assets as a result of Warehouse Automation project	—	(14)	—	(14)
Accelerated depreciation of assets as a result of Warehouse Automation project	—	(80)	—	(80)
Adjusted income tax provision	\$(2,566)	\$(3,902)	\$(3,981)	\$(10,557)

LIQUIDITY AND CAPITAL RESOURCES

The following table presents information regarding our cash flows for the six months ended June 30, 2018 and 2017:

(In thousands)	2018	2017
Net cash flows from operating activities	\$ 110,876	\$ 103,599
Net cash flows from investing activities	(77,793)	(85,292)
Net cash flows from financing activities	4,457	(32,789)

Cash Flows Summary

Net cash flows provided by operating activities for the six months ended June 30, 2018 increased by \$7.3 million compared to the same period in 2017. The increase in operating cash flows was driven by an increase of \$12.6 million from changes in working capital primarily as the result of a decrease in accounts receivable caused by the sale of \$22.0 million of receivables at the end of the second quarter to an unrelated third-party financial institution, as discussed in Note 1 to the Consolidated Financial Statements. In addition, net cash flows from operating activities increased due to a change in taxes receivable of \$7.3 million as the result of an increase in cash received from income tax refunds. These favorable variances were partially offset by a \$12.5 million decrease in net earnings, after adjusting for non-cash related items.

Net cash flows used for investing activities decreased by \$7.5 million primarily due to a decrease in cash paid for plant and equipment in the six months ended June 30, 2018 compared to the same period in 2017. In addition to cash paid for plant and equipment, we also incurred \$88.9 million of non-cash additions in the 2018 period, which is largely associated with our Shelby expansion project.

Net cash flows provided by financing activities were \$4.5 million for the first six months of 2018, and were largely driven by net borrowings of \$5.0 million on our revolving credit facilities. Borrowings and repayments on our credit facilities are presented gross on our Consolidated Statements of Cash Flows. Net cash flows used for financing activities were \$32.8 million for the first six months of 2017, due largely to \$4.9 million in repurchases of our outstanding common stock, pursuant to our stock repurchase program, as well as net repayments of \$27.0 million on our revolving credit facilities.

Capital Resources

Due to the competitive and cyclical nature of the markets in which we operate, there is uncertainty regarding the amount of cash flows we will generate during the next twelve months. However, we believe that our cash flows from operations, our cash on hand, and our borrowing capacity under our senior secured revolving credit facilities will be adequate to fund our debt service requirements

and provide cash required to support our ongoing operations, capital expenditures, and working capital needs for the next twelve months.

We may choose to refinance all or a portion of our indebtedness on or before maturity. We cannot be certain that we will be able to refinance any of our indebtedness on commercially reasonable terms or at all.

Capital Expenditures

In addition to ongoing maintenance and repair costs, we make capital expenditures to increase our operating capacity and efficiency, improve safety at our facilities, and comply with environmental laws. During the six months ended June 30, 2018, excluding capitalized interest of \$3.2 million, we spent \$164.3 million on capital expenditures, which included \$155.4 million of capital spending on strategic projects and other projects designed to reduce future manufacturing costs and provide a positive return on investment. During the six months ended June 30, 2017, we spent \$87.6 million on capital expenditures, excluding capitalized interest of \$1.9 million, which included \$69.5 million of capital spending on strategic projects and other projects expected to reduce future manufacturing costs and provide a positive return on investment.

Debt Arrangements

Our annual debt service obligation, consisting of cash payments for interest on the 2013 Notes and the 2014 Notes, is estimated to be \$28.5 million for 2018. The terms of the 2013 Notes limit our ability and the ability of any restricted subsidiaries to borrow money, pay dividends, redeem or repurchase capital stock, make investments, sell assets, create restrictions on the payment of dividends or other amounts to us from any restricted subsidiaries, enter into transactions with affiliates, enter into sale and lease back transactions, create liens, and consolidate, merge or sell all or substantially all of our assets. The terms of the 2014 Notes limit our ability and the ability of any restricted subsidiaries to incur certain liens, engage in sale and leaseback transactions and consolidate, merge with, or convey, transfer, or lease substantially all of our or their assets to another person.

Credit Arrangements

Our revolving credit facilities contain various loan covenants that restrict our ability and that of our subsidiaries to take certain actions, including, incurrence of indebtedness, creation of liens, mergers or consolidations, dispositions of assets, repurchase or redemption of capital stock, making certain investments, entering into certain transactions with affiliates or changing the nature of their business. In addition, the revolving credit facilities contain financial covenants that require us to maintain a consolidated total leverage ratio in an amount not to exceed 4.50 to 1.00 in 2018, 4.25 to 1.00 in 2019, and 4.00 to 1.00 thereafter (subject to certain exceptions with respect to acquisitions in excess of an agreed threshold amount) and a consolidated interest coverage ratio in an amount not less than 1.75 to 1.00 through 2020 and 2.25 to 1.00 thereafter.

As of June 30, 2018, our consolidated total leverage ratio for the most recent four quarters was 3.95 to 1.0 and our consolidated interest coverage ratio was 2.5 to 1.0. Based on our current financial projections and also taking into account certain actions that are available to us to enhance our compliance with these covenants, we expect to remain in compliance with them for the foreseeable future. However, if market conditions deteriorate more than we expect or our results of operations or financial position are negatively affected by other factors currently not anticipated, we may not be able to remain in compliance. There can be no assurance that we will be able to remain in compliance with either of these covenants, and if we are unable to do so, it would be necessary to seek amendments to the affected covenants from our lenders, which, if obtained, could require payment of additional fees, increased interest rates or other conditions or restrictions.

See Note 7, "Debt" to the condensed notes to the consolidated financial statements included in this Report for additional discussion of our revolving credit facilities.

CONTRACTUAL OBLIGATIONS

As of June 30, 2018, there were no significant changes to the contractual obligations table disclosed in our Annual Report on Form 10-K for the year ended December 31, 2017.

OFF-BALANCE SHEET ARRANGEMENTS

We currently are not a party to off-balance sheet arrangements that would require disclosure under this section.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The preparation of financial statements in accordance with GAAP requires our management to select and apply accounting policies that best provide the framework to report our results of operations and financial position. The selection and application of those policies requires management to make difficult, subjective and complex judgments concerning reported amounts of revenue and expenses during the reporting period and the reported amounts of assets and liabilities at the date of the financial statements. As a result, it is possible that materially different amounts would be reported under different conditions or using different assumptions.

As of June 30, 2018, there have been no significant changes with regard to the critical accounting policies disclosed in our Annual Report on Form 10-K for the year ended December 31, 2017.

See Note 2 "Recently Adopted and New Accounting Standards" to the Consolidated Financial Statements included in Item 1 of this Quarterly Report on Form 10-Q for additional information regarding recently adopted and new accounting pronouncements.

ITEM 3.

Quantitative
and

Qualitative
Disclosures

About

Market Risk

Interest Rate Risk

Our exposure to market risks on financial instruments includes interest rate risk on our secured revolving credit facilities. As of June 30, 2018, there were \$160.0 million in borrowings outstanding under our revolving credit facilities. The interest rates applied to borrowings under the credit facilities are adjusted often and therefore react quickly to any movement in the general trend of market interest rates. For example, a one percentage point increase or decrease in interest rates, based on assumed outstanding credit facilities' borrowings of \$160.0 million, would have an approximate \$1.6 million annual effect on interest expense. During the first half of 2018, we reduced our short-term interest rate risk through the use of a short-term LIBOR Rate option for \$60.0 million of our total outstanding credit facilities' borrowings balance of \$160.0 million. We currently do not attempt to alleviate the effects of short-term interest rate fluctuations on our credit facility borrowings through the use of derivative financial instruments.

Commodity Risk

We are exposed to market risk for changes in natural gas commodity pricing, which we partially mitigate through the use of firm price contracts for a portion of our natural gas requirements for our manufacturing facilities. As of June 30, 2018, these contracts covered approximately 29% of our expected average monthly natural gas requirements for the remainder of 2018.

Foreign Currency Risk

We have minimal foreign currency exchange risk. Nearly all of our international sales are denominated in U.S. dollars.

ITEM 4.

Controls

and

Procedures

We maintain "disclosure controls and procedures," as such term is defined in Rule 13a-15(e) under the Securities and Exchange Act of 1934, or the Exchange Act, that are designed to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in SEC rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer, or CEO, and Chief Financial Officer, or CFO, as appropriate, to allow timely decisions regarding required disclosure. In designing and evaluating our disclosure controls and procedures, management recognized that disclosure controls and procedures, no matter how well conceived and

operated, can provide only reasonable, not absolute, assurance that the objectives of the disclosure controls and procedures are met. Additionally, in designing disclosure controls and procedures, our management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible disclosure controls and procedures. The design of disclosure controls and procedures is also based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions.

Subject to the limitations noted above, our management, with the participation of our CEO and CFO, has evaluated the effectiveness of the design and operation of our disclosure controls and procedures as of the end of the second quarter of 2018. Based on that evaluation, the CEO and CFO have concluded that, as of June 30, 2018, our disclosure controls and procedures were effective to meet the objective for which they were designed and operated at the reasonable assurance level.

Changes in Internal Controls

There was no change in our internal control over financial reporting during our most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Part II

ITEM 1.

Legal

Proceedings

We may from time to time be involved in claims, proceedings and litigation arising from our business and property ownership. We believe, based on currently available information, that the results of such proceedings, in the aggregate, will not have a material adverse effect on our financial condition.

ITEM 1A.

Risk

Factors

There are no material changes from the risk factors previously disclosed in our Annual Report on Form 10-K for the year ended December 31, 2017. See Part I, Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2017, entitled "Risk Factors."

ITEM 2.

Unregistered

Sales of

Equity

Securities

and Uses of

Proceeds

Issuer Purchases of Equity Securities

Refer to the "Stockholders' Equity" section of Note 1, "Nature of Operations and Basis of Presentation," to the consolidated financial statements included in this Report for discussion of issuer purchases of equity securities. We did not repurchase shares during the three months ended June 30, 2018.

ITEM 6.
Exhibits

EXHIBIT NUMBER	DESCRIPTION
(31)	<u>Rule 13a-14(a)/15d-14(a) Certifications.</u>
(32)**	<u>Furnished statements of the Chief Executive Officer and Chief Financial Officer under 18 U.S.C Section 1350.</u>
10(i) ¹	<u>Clearwater Paper Corporation Deferred Compensation Plan for Directors, Amended and Restated, effective as of January 1, 2018.</u>
10(ii)	<u>Amendment No. 2 to the Credit Agreement and Amendment to the Collateral Agreement dated as of June 27, 2018 by and among Clearwater Paper Corporation, the lenders signatory thereto and Wells Fargo Bank, National Association.</u>
10(iii)	<u>Amendment No. 2 to the Credit Agreement and Amendment to the Collateral Agreement dated as of June 27, 2018 by and among Clearwater Paper Corporation, the lenders signatory thereto and Northwest Farm Credit Services, PCA.</u>
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema.
101.CAL	XBRL Taxonomy Extension Calculation Linkbase.
101.DEF	XBRL Taxonomy Extension Definition Linkbase.
101.LAB	XBRL Taxonomy Extension Label Linkbase.
101.PRE	XBRL Taxonomy Extension Presentation Linkbase.

In accordance with Item 601(b)(32)(ii) of Regulation S-K and SEC Release No. 34-47986, the certifications furnished in Exhibit 32 hereto are deemed to accompany this Form 10-Q and will not be deemed “filed” for purposes of Section 18 of the Exchange Act. Such certifications will not be deemed to be incorporated by reference into any filing under the Securities Act or the Exchange Act.

¹ Management contract or compensatory plan, contract or arrangement.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

CLEARWATER PAPER
CORPORATION
(Registrant)

August 6, 2018 By/s/ JOHN D. HERTZ
John D. Hertz
Senior Vice President, Finance and
Chief Financial Officer
(Duly Authorized Officer; Principal
Financial Officer)

August 6, 2018 By/s/ ROBERT N. DAMMARELL
Robert N. Dammarell
Vice President, Corporate Controller
(Duly Authorized Officer; Principal
Accounting Officer)