

LOUISIANA-PACIFIC CORP  
Form 10-Q  
August 04, 2006

# UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

## FORM 10-Q

Quarterly Report Under Section 13 or 15(d)  
of the Securities Exchange Act of 1934

For Quarterly Period Ended June 30, 2006

Commission File Number 1-7107

### LOUISIANA-PACIFIC CORPORATION

(Exact name of registrant as specified in its charter)

**DELAWARE**

(State or other jurisdiction of  
incorporation or organization)

**93-0609074**

(IRS Employer Identification No.)

**414 Union Street, Nashville, TN 37219**

(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: **(615) 986-5600**

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 ☐

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Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer ☒

Accelerated filer ☐

Non-accelerated filer ☐

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

Yes ☐ No ☒

Indicate the number of shares outstanding of each of the issuer's classes of common stock: xxx,xxx,xxx shares of Common Stock, \$1 par value, outstanding as of August 4, 2006.

Except as otherwise specified and unless the context otherwise requires, references to LP, the Company, we, us, and our refer to Louisiana-Pacific Corporation and its subsidiaries.

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**ABOUT FORWARD-LOOKING STATEMENTS**

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Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934 provide a safe harbor for forward-looking statements to encourage companies to provide prospective information about their businesses and other matters as long as those statements are identified as forward-looking and are accompanied by meaningful cautionary statements identifying important factors that could cause actual results to differ materially from those discussed in the statements. This report contains, and other reports and documents filed by us with the Securities and Exchange Commission may contain, forward-looking statements. These statements are or will be based upon the beliefs and assumptions of, and on information available to, our management.

The following statements are or may constitute forward-looking statements: (1) statements preceded by, followed by or that include words like may, will, could, should, believe, expect, anticipate, intend, plan, estimate, potential, continue or future or the negative thereof and (2) other statements regarding matters that are not historical facts, including without limitation, plans for product development, forecasts of future costs and expenditures, possible outcomes of legal proceedings, completion of anticipated asset sales and the adequacy of reserves for loss contingencies.

Factors that could cause actual results to differ materially from those expressed or implied by the forward-looking statements include, but are not limited to the following:

- changes in general economic conditions;
- changes in the cost and availability of capital;
- changes in the level of home construction activity;
- changes in competitive conditions and prices for our products;
- changes in the relationship between supply of and demand for building products, including the effects of industry-wide increases in manufacturing capacity;
- changes in the relationship between supply of and demand for raw materials, including wood fiber and resins, used in manufacturing our products;
- changes in the cost of and availability of energy, primarily natural gas, electricity and diesel fuel;
- changes in other significant operating expenses;
- changes in exchange rates between the U.S. dollar and other currencies, particularly the Canadian dollar, EURO and the Chilean peso;
- changes in general and industry-specific environmental laws and regulations;
- changes in circumstances giving rise to environmental liabilities or expenditures;
- the resolution of product-related litigation and other legal proceedings; and
- acts of God or public authorities, war, civil unrest, fire, floods, earthquakes and other matters beyond our control.

In addition to the foregoing and any risks and uncertainties specifically identified in the text surrounding forward-looking statements, any statements in the reports and other documents filed by us with the Commission that warn of risks or uncertainties associated with future results, events or circumstances identify important factors that could cause actual results, events and circumstances to differ materially from those reflected in the forward-looking statements.

### ABOUT THIRD PARTY INFORMATION

### ABOUT FORWARD-LOOKING STATEMENTS

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In this report, we rely on and refer to information regarding industry data obtained from market research, publicly available information, industry publications, U.S. government sources and other third parties. Although we believe the information is reliable, we cannot guarantee the accuracy or completeness of the information and have not independently verified it.

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## Item 1. Financial Statements.

CONSOLIDATED STATEMENTS OF INCOME  
LOUISIANA-PACIFIC CORPORATION AND SUBSIDIARIES

(AMOUNTS IN MILLIONS EXCEPT PER SHARE AMOUNTS) (UNAUDITED)

	Quarter Ended June 30,		Six Months Ended June 30,	
	2006	2005	2006	2005
Net sales	\$ 652.7	\$ 692.0	\$ 1,331.0	\$ 1,353.4
Operating costs and expenses:				
Cost of sales	505.7	463.5	991.2	889.1
Depreciation, amortization and cost of timber harvested	32.4	32.4	66.9	65.3
Selling and administrative	40.8	36.1	82.8	73.7
(Gain) loss on sale or impairment of long-lived assets	0.1	(0.7)	)	(0.9)
Other operating credits and charges, net		1.4	0.1	1.1
Total operating costs and expenses	579.0	532.7	1,141.0	1,028.3
Income from operations	73.7	159.3	190.0	325.1
Non-operating income (expense):				
Foreign currency exchange (loss) gain	(10.6)	) (1.4)	) (8.5)	) (2.0)
Interest expense, net of capitalized interest	(14.3)	) (15.3)	) (27.7)	) (31.0)
Investment income	24.3	16.9	47.3	32.4
Total non-operating income (expense)	(0.6)	) 0.2	11.1	(0.6)
Income before taxes and equity in earnings of unconsolidated affiliates	73.1	159.5	201.1	324.5
Provision for income taxes	18.3	55.2	62.6	115.5
Equity in earnings of unconsolidated affiliates	(0.3)	) (0.1)	) (1.5)	) (0.8)
Income from continuing operations	55.1	104.4	140.0	209.8
Discontinued operations:				
Loss from discontinued operations before taxes		(6.6)	) (2.0)	) (12.6)
Income tax benefit		(2.5)	) (0.8)	) (4.8)
Loss from discontinued operations		(4.1)	) (1.2)	) (7.8)
Net income	\$ 55.1	\$ 100.3	\$ 138.8	\$ 202.0
Net income per share of common stock (basic):				
Income from continuing operations	\$ 0.52	\$ 0.94	\$ 1.32	\$ 1.90
Loss from discontinued operations		(0.04)	) (0.01)	) (0.07)
Net income per share - basic	\$ 0.52	\$ 0.90	\$ 1.31	\$ 1.83
Net income per share of common stock (diluted):				
Income from continuing operations	\$ 0.52	\$ 0.94	\$ 1.32	\$ 1.89
Loss from discontinued operations		(0.04)	) (0.01)	) (0.07)
Net income per share - diluted	\$ 0.52	\$ 0.90	\$ 1.31	\$ 1.82
Cash dividends per share of common stock	\$ 0.15	\$ 0.125	\$ 0.30	\$ 0.225
Average shares of stock outstanding - basic	105.3	110.9	105.6	110.5
Average shares of stock outstanding - diluted	105.8	111.5	106.2	111.3

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



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CONDENSED CONSOLIDATED BALANCE SHEETS  
LOUISIANA-PACIFIC CORPORATION AND SUBSIDIARIES

(AMOUNTS IN MILLIONS) (UNAUDITED)

	June 30, 2006	December 31, 2005
<b>ASSETS</b>		
Cash and cash equivalents	\$ 376.1	\$ 607.6
Short-term investments	834.3	717.3
Receivables, net	128.4	146.8
Inventories	255.8	240.3
Prepaid expenses and other current assets	15.8	14.4
Deferred income taxes	30.5	
Current portion of notes receivable from asset sales		70.8
Total current assets	1,640.9	1,797.2
Timber and timberlands	92.1	92.9
Property, plant and equipment	1,898.3	1,848.9
Accumulated depreciation	(1,128.3)	(1,065.6)
Net property, plant and equipment	770.0	783.3
Goodwill, net of amortization	273.5	273.5
Notes receivable from asset sales	333.0	333.0
Long-term investments	64.5	13.5
Restricted cash	39.6	55.6
Investments in and advances to affiliates	221.0	211.0
Other assets	36.0	38.0
Total assets	\$ 3,470.6	\$ 3,598.0
<b>LIABILITIES AND EQUITY</b>		
Current portion of long-term debt	\$ 0.6	\$ 18.9
Current portion of limited recourse notes payable		69.7
Accounts payable and accrued liabilities	227.1	245.5
Current portion of contingency reserves	12.0	12.0
Total current liabilities	239.7	346.1
Long-term debt, excluding current portion:		
Limited recourse notes payable	326.8	326.8
Other long-term debt	319.9	408.0
Total long-term debt, excluding current portion	646.7	734.8
Contingency reserves, excluding current portion	24.1	31.4
Other long-term liabilities	62.3	65.8
Deferred income taxes	365.1	377.0
<b>Commitments and contingencies</b>		
<b>Stockholders' equity:</b>		
Common stock	116.9	116.9
Additional paid-in capital	433.4	435.5
Retained earnings	1,916.8	1,809.7
Treasury stock	(265.5)	(257.0)
Accumulated comprehensive loss	(68.9)	(62.2)
Total stockholders' equity	2,132.7	2,042.9
Total liabilities and equity	\$ 3,470.6	\$ 3,598.0

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





**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**LOUISIANA-PACIFIC CORPORATION AND SUBSIDIARIES**

(AMOUNTS IN MILLIONS) (UNAUDITED)

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	Six Months Ended June 30,	
	2006	2005
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Net income	\$ 138.8	\$ 202.0
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation, amortization and cost of timber harvested	66.9	66.4
Earnings of unconsolidated affiliates	(1.5 )	0.8
(Gain) loss on sale or impairment of long-lived assets	(0.4 )	
Tax effect of exercise of stock options		3.5
Stock-based compensation related to stock plans	3.2	
Excess tax benefits from stock-based compensation	(3.3 )	
Exchange loss on remeasurement	15.8	6.3
Cash settlement of contingencies	(7.7 )	(4.7 )
Other adjustments, net	0.2	(2.7 )
Decrease in receivables	20.5	5.6
Increase in inventories	(16.6 )	(9.6 )
Increase in prepaid expenses	(2.0 )	(0.1 )
Decrease in accounts payable and accrued liabilities	(9.8 )	(50.9 )
Increase (decrease) in deferred income taxes	(48.0 )	34.7
Net cash provided by operating activities	156.1	251.3
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Property, plant and equipment additions	(64.7 )	(67.0 )
Proceeds from asset sales	1.5	30.1
Receipt of proceeds from notes receivable	70.8	
Investments and advances to joint ventures	(8.8 )	(52.1 )
Proceeds from sales of investments	3,439.3	2,421.4
Cash paid for purchase of investments	(3,602.3 )	(2,452.8 )
Decrease (increase) in restricted cash under letters of credit	16.0	(0.9 )
Other investing activities, net		0.1
Net cash used in investing activities	(148.2 )	(121.2 )
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Repayment of debt	(189.1 )	
Sale of common stock under equity plans	5.5	8.7
Excess tax benefits from stock-based compensation	3.3	
Purchase of treasury stock	(22.3 )	
Payment of cash dividends	(31.8 )	(24.9 )
Net cash used in financing activities	(234.4 )	(16.2 )
<b>EFFECT OF EXCHANGE RATE ON CASH AND CASH EQUIVALENTS:</b>		
	(5.0 )	(2.1 )
Net increase (decrease) in cash and cash equivalents	(231.5 )	111.8
Cash and cash equivalents at beginning of period	607.6	544.7
Cash and cash equivalents at end of period	\$ 376.1	\$ 656.5

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

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY  
LOUISIANA-PACIFIC CORPORATION AND SUBSIDIARIES  
(AMOUNTS IN MILLIONS) (UNAUDITED)

	Common Stock Shares	Amount	Treasury Stock Shares	Amount	Additional Paid-in Capital	Retained Earnings	Accumulated Comprehensive Loss	Total Stockholders' Equity
Balance, December 31, 2005	116.9	\$ 116.9	11.2	\$ (257.0)	) \$ 435.5	\$ 1,809.7	\$ (62.2)	) \$ 2,042.9
Net income						138.8		138.8
Issuance of shares for employee stock plans and other purposes and other transactions			(0.6)	) 13.8	(7.5)			6.3
Purchase of shares for treasury			1.2	(22.3)	)			(22.3)
Stock-based compensation related to stock plans					2.1			2.1
Excess tax benefits of stock-based compensation					3.3			3.3
Cash dividends						(31.7)		(31.7)
Other comprehensive loss							(6.7)	(6.7)
Balance, June 30, 2006	116.9	\$ 116.9	11.8	\$ (265.5)	) \$ 433.4	\$ 1,916.8	\$ (68.9)	) \$ 2,132.7

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

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME  
LOUISIANA-PACIFIC CORPORATION AND SUBSIDIARIES  
(AMOUNTS IN MILLIONS) (UNAUDITED)

	Quarter Ended June 30,		Six Months Ended June 30,	
	2006	2005	2006	2005
Net income	\$ 55.1	\$ 100.3	\$ 138.8	\$ 202.0
Other comprehensive income (loss), net of tax				
Foreign currency translation adjustments	(3.8 )		(7.0 )	0.4
Unrealized gain (loss) on marketable securities	(0.2 )	0.1	(0.2 )	0.2
Unrealized gain (loss) on derivative instruments	0.2	0.5	0.5	(0.8 )
Other comprehensive income (loss), net of tax	(3.8 )	0.6	(6.7 )	(0.2 )
Comprehensive income, net of tax	\$ 51.3	\$ 100.9	\$ 132.1	\$ 201.8

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

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## NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

### NOTE 1 BASIS FOR PRESENTATION

The accompanying unaudited consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q and, in the opinion of management, include all adjustments (consisting of normal recurring adjustments, except for other operating credits and charges, net referred to in Note 7) necessary to present fairly, in all material respects, the consolidated financial position, results of operations and cash flows of LP and its subsidiaries for the interim periods presented. Results of operations for interim periods are not necessarily indicative of results to be expected for an entire year. These condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and the notes thereto included in LP's Annual Report on Form 10-K for the year ended December 31, 2005.

#### *Stock-Based Compensation*

Effective January 1, 2006, LP adopted the fair value recognition provisions of Statement of Financial Accounting Standards (SFAS) No. 123 (revised 2004), Share-Based Payment (SFAS 123R), using the modified prospective transition method and therefore has not restated results for prior periods. Under this transition method, stock-based compensation expense for the six months ended June 30, 2006 includes compensation expense for all stock-based compensation awards granted prior to, but not yet vested as of January 1, 2006, based on the grant date fair value estimated in accordance with the original provision of SFAS No. 123, Accounting for Stock-Based Compensation (SFAS 123). Compensation expense for all stock-based compensation awards granted after January 1, 2006 is based on the grant-date fair value estimated in accordance with the provisions of SFAS 123R. LP recognizes these compensation costs on a straight-line basis over the requisite service period of the award, which is generally the option vesting term of three years. Prior to the adoption of SFAS 123R, LP recognized stock-based compensation expense in accordance with Accounting Principles Board (APB) Opinion No. 25, Accounting for Stock Issued to Employees (APB 25). In March 2005, the Securities and Exchange Commission (the SEC) issued Staff Accounting Bulletin No. 107 (SAB 107) regarding the SEC's interpretation of SFAS 123R and the valuation of share-based payments for public companies. LP has applied the provisions of SAB 107 in its adoption of SFAS 123R. See Note 2 to the Condensed Consolidated Financial Statements for a further discussion of stock-based compensation.

### NOTE 2 STOCK-BASED COMPENSATION

At June 30, 2006, LP has stock-based employee compensation plans as described below. The total compensation expense related to all of LP's stock-based compensation plans was \$1.8 million and \$3.3 million for the quarter and six month period ended June 30, 2006. Prior to January 1, 2006, LP accounted for these plans under the recognition and measurement provisions of APB 25. Accordingly, LP generally recognized compensation expense only when it modified stock option terms (as required by Financial Interpretation No. 44 (FIN 44)) or granted restricted stock units or restricted stock. Any resulting expense was recognized ratably over the associated service period, which was generally the vesting term of the award.

Prior to January 1, 2006, LP provided pro forma disclosure amounts in accordance with SFAS No. 148, Accounting for Stock-Based Compensation Transition and Disclosure (SFAS 148), as if the fair value method defined by SFAS 123 had been applied to its stock-based compensation.

Effective January 1, 2006, LP adopted the fair value recognition provisions of SFAS 123R, using the modified prospective transition method and therefore has not restated results for prior periods. Under this transition method, stock-based compensation expense for the first six months of 2006 includes compensation expense for all stock-based compensation awards granted prior to, but not yet vested as of, January 1, 2006, based on the grant date fair value estimated in accordance with the original provisions of SFAS 123. Compensation expense for all stock-based compensation awards granted after January 1, 2006 is based on the grant date fair value estimated in accordance with the provisions of SFAS 123R. LP recognizes these compensation costs net of an estimated forfeiture rate and recognizes the compensation costs for only those shares expected to vest on a straight-line basis over the requisite service period of the award, which is generally the vesting term of three years. LP estimated the forfeiture rate for the first six months of 2006 based on its historical experience during the preceding two fiscal years.

As a result of adopting SFAS 123R, income before income taxes and net income for the quarter ended June 30, 2006 was \$1.1 million and \$0.7 million lower than if we had continued to account for stock-based compensation under APB 25. Income before income taxes and net income for the six month period ended June 30, 2006 was \$2.0 million and \$1.2 million lower than if we had continued to account for stock-based compensation under APB 25. The impact on both basic and diluted earnings per share for the quarter ended and six month period ended June 30, 2006 was a decrease of \$0.01 per share. In addition, prior to the adoption of SFAS 123R, LP presented the tax benefit of stock option exercises as operating cash flows. Upon the adoption of SFAS 123R, tax benefits resulting from tax deductions in excess of the compensation cost recognized for those options are classified as financing cash flows.

The following table illustrates the effect (in millions, except per share amounts) on net income and basic and diluted earnings per share as if the fair value recognition provisions of SFAS 123 had been applied to all outstanding and unvested awards in the quarter ended and six month period ended June 30, 2005. For purposes of this pro forma disclosure, the value of the options was estimated using the Black-Scholes option-pricing model with the following weighted average assumptions used for grants during the six month period ended June 30, 2005: a risk free interest rate of 3.8%; an expected volatility factor for the market price of the Company's common stock of 51.7%; a dividend yield of 1.6%; and an expected life of 4 years. The weighted-average estimated fair value of the options granted during the six month period ended June 30, 2005 was \$10.62.

Dollar amounts in millions, except per share amounts	Quarter Ended June 30, 2005	Six Months Ended June 30, 2005
Net income, as reported	\$ 100.3	\$ 202.0
Add: Stock-based employee compensation included in reported net income, net of related income tax effects	0.3	0.6
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	(0.6)	(1.3)
Pro forma net income	\$ 100.0	\$ 201.3
Net income per share basic, as reported	\$ 0.90	\$ 1.83
Net income per share diluted, as reported	\$ 0.90	\$ 1.82
Net income per share basic, pro forma	\$ 0.90	\$ 1.82
Net income per share diluted, pro forma	\$ 0.90	\$ 1.81

#### Stock Compensation Plans

LP grants options and stock settled stock appreciation rights (SSARs) to key employees and directors to purchase LP common stock. On exercise or issuance, LP generally issues these shares from treasury. The options and SSARs are granted at market price at the date of grant. For employees, options and SSARs become exercisable over three years and expire ten years after the date of grant. For directors, 10% of these options become exercisable every three months following the grant. At June 30, 2006, 7,845,684 shares were available under the current stock award plans for stock-based awards. For the six month period ended June 30, 2006, the fair value of the options granted was estimated using the Black-Scholes option-pricing model with the following weighted average assumptions: a risk free interest rate of 4.5%; an expected volatility factor for the market price of the Company's common stock of 45.2% (based upon historical volatility over the expected life); a dividend yield of 1.9%; and an expected life of 4 years (based upon historical experience). The weighted-average fair value of each option granted during the six month period ended June 30, 2006 was \$10.26.

The following table summarizes stock options and stock settled stock appreciation rights outstanding as of June 30, 2006 as well as activity during the six month period then ended.



Share amounts in thousands	Options/ SSARs	Weighted Average Exercise Price	Weighted Average Contractual Term (in years)	Aggregate Intrinsic Value (in millions)
Outstanding options				
Options outstanding at January 1, 2006	2,135	\$ 16.89		
Options granted	575	\$ 28.54		
Options exercised	(526)	) \$ 10.54		
Options cancelled	(10)	) \$ 25.13		
Options outstanding at June 30, 2006	2,174	\$ 21.48	6.73	\$ 6.8
Vested and expected to vest at June 30, 2006	2,168	\$ 21.47	6.73	\$ 6.8
Options exercisable at June 30, 2006	1,298	\$ 17.41	5.09	\$ 6.7

The aggregate intrinsic value in the table above represents the total pre-tax intrinsic value (the difference between LP's closing stock price on the last trading day of the second quarter of 2006 and the exercise price, multiplied by the number of in-the-money options and SSARs) that would have been received by the holders had all holders exercised their awards on June 30, 2006. This amount changes based on the market value of LP's stock as reported by the New York Stock Exchange. Total intrinsic value of options exercised for the six month period ended June 30, 2006 was \$9.2 million.

As of June 30, 2006, there was \$7.4 million of total unrecognized compensation costs related to stock options and SSARs. These costs are expected to be recognized over a weighted-average period of 1.4 years.

Cash received from option exercises for the first six months of 2006 was \$5.5 million. The tax benefit realized for the tax deduction from option exercises of the share-based payment awards totaled \$3.3 million for the six month period ended June 30, 2006.

#### ***INCENTIVE SHARE AWARDS***

LP has granted incentive share stock awards (restricted stock units) to selected senior executives as allowed under the current stock award plans. The awards entitle the participant to receive a specified number of shares of LP common stock at no cost to the participant. For all years prior to 2005, these awards vest over a five-year period, subject to vesting acceleration upon the achievement of various stock price targets. The stock price targets were reached for all grants except for fifty percent of the 2004 grants. For the remaining awards granted in 2004, if LP's stock trades at or above \$29.78 per share for five consecutive days prior to the end of the five-year period, the remaining awards will automatically vest at the next anniversary of the grant. The 2005 and 2006 awards for employees vest three years from the date of grant. The market value of these grants approximates the fair value. LP recorded compensation expense related to these awards in the second quarter and first six months of 2006 of \$0.3 million and \$0.5 million. As of June 30, 2006, there was \$2.4 million of total unrecognized compensation cost related to unvested incentive share awards. This expense will be recognized over a weighted-average period of 2.2 years.

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The following table summarizes incentive share awards outstanding as of June 30, 2006 as well as activity during the six months then ended.

	Shares	Weighted Average Contractual Term (in years)	Aggregate Intrinsic Value (in millions)
Incentive share awards outstanding at January 1, 2006	95,701		
Incentive shares awards granted	51,850		
Incentive share awards vested	0		
Incentive share awards cancelled	(2,260 )		
Incentive share awards outstanding at June 30, 2006	145,291	2.23	\$ 3.2
Vested and expected to vest at June 30, 2006	145,291	2.23	\$ 3.2
Incentive share awards exercisable at June 30, 2006	0	0	\$

## Restricted Stock

Beginning in 2005, LP began granting restricted stock to certain key executive employees. The shares vest three years from the date of grant. During the vesting period, the participants have voting rights and receive dividends, but the shares may not be sold, assigned, transferred, pledged or otherwise encumbered. Additionally, granted but unvested shares are forfeited upon termination of employment. The fair value of the restricted shares on the date of the grant is amortized ratably over the vesting period. As of June 30, 2006, there was \$2.6 million of total unrecognized compensation costs related to restricted stock. This expense will be recognized over the next 2.1 years.

The following table summarizes the restricted stock outstanding as of June 30, 2006 as well as activity during the six months then ended.

	Six Months Ended June 30, 2006	
	Number of Shares	Weighted Average Grant Date Fair Value
Outstanding restricted shares		
Restricted stock awards outstanding at January 1, 2006	65,600	\$ 27.04
Restricted stock awards granted	66,650	\$ 28.90
Restrictions lapsing		
Restricted stock awards cancelled		
Restricted stock awards at June 30, 2006	132,250	\$ 27.98

LP recorded compensation expense related to these awards in the second quarter and first six months of 2006 of \$0.3 million and \$0.6 million.

LP annually grants to each director restricted stock or restricted stock. As of June 30, 2006, LP has 47,697 shares (or restricted stock units) outstanding under this program. Compensation expense recognized in 2006 related to these grants was \$0.2 million.

## NOTE 3 EARNINGS PER SHARE

Basic net income per share is computed using the weighted-average number of common shares outstanding during the period. Diluted net income per share is computed using the weighted-average number of common shares and dilutive potential common shares outstanding during the period. Dilutive potential common shares primarily consist of employee stock options, SSARs, restricted stock units and restricted common stock.

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SFAS No. 128, Earnings per Share, requires that employee equity share options, non-vested shares and similar equity instruments granted by the Company be treated as potential common shares outstanding in computing diluted earnings per share. Diluted shares outstanding include the dilutive effect of in-the-money options, which is calculated based on the average share price for each fiscal period using the treasury stock method. Under the treasury stock method, the amount the employee must pay for exercising stock options, the amount of compensation cost for future service that the Company has not yet recognized, and the amount of tax benefits that would be recorded in additional paid-in capital when the award becomes deductible are assumed to be used to repurchase shares.

Dollar and share amounts in millions, except per share amounts	Quarter Ended June 30,		Six Months Ended June 30,	
	2006	2005	2006	2005
Numerator:				
Income attributed to common shares:				
Income from continuing operations	\$ 55.1	\$ 104.4	\$ 140.0	\$ 209.8
Loss from discontinued operations		(4.1 )	(1.2 )	(7.8 )
Net income	\$ 55.1	\$ 100.3	\$ 138.8	\$ 202.0
Denominator:				
Basic - weighted average common shares outstanding	105.3	110.9	105.6	110.5
Dilutive effect of stock plans	0.5	0.6	0.6	0.8
Diluted shares outstanding	105.8	111.5	106.2	111.3
Basic earnings per share:				
Income from continuing operations	\$ 0.52	\$ 0.94	\$ 1.32	\$ 1.90
Loss from discontinued operations		(0.04 )	(0.01 )	(0.07 )
Net income per share	\$ 0.52	\$ 0.90	\$ 1.31	\$ 1.83
Diluted earnings per share:				
Income from continuing operations	\$ 0.52	\$ 0.94	\$ 1.32	\$ 1.89
Loss from discontinued operations		(0.04 )	(0.01 )	(0.07 )
Net income per share	\$ 0.52	\$ 0.90	\$ 1.31	\$ 1.82

Stock options to purchase approximately 0.9 million shares at June 30, 2006 and 0.3 million shares at June 30, 2005 were considered anti-dilutive or not in-the-money for purposes of LP's earnings per share calculation.

## NOTE 4 INVENTORIES

Inventories are valued at the lower of cost or market. Inventory cost includes materials, labor and operating overhead. The LIFO (last-in, first-out) method is used for certain log inventories with remaining inventories valued at FIFO (first-in, first-out) or average cost. The major types of inventories are as follows (work in process is not material):

Dollar amounts in millions	June 30, 2006	December 31, 2005
Logs	\$ 57.6	\$ 76.3
Other raw materials	40.5	38.8
Finished products	153.3	120.7
Supplies	8.3	8.4
LIFO reserve	(3.9 )	(3.9 )
Total	\$ 255.8	\$ 240.3

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# NOTE 5 BUSINESSES HELD FOR SALE AND DIVESTITURES

At June 30, 2006, LP had no operations classified as discontinued. For the first six months of 2006, the loss from discontinued operations relates to residual charges from previously discontinued operations. For the first six months of 2005, LP's discontinued operations included two lumber mills and its vinyl operations.

Sales and income (loss) for these businesses are as follows:

Dollar amounts in millions	Quarter Ended June 30,		Six Months Ended June 30,	
	2006	2005	2006	2005
Sales	\$ 0.4	\$ 44.6	\$ (0.3 )	\$ 82.7
Loss from discontinued operations, net of tax	\$	\$ (4.1 )	\$ (1.2 )	\$ (7.8 )

In the first quarter of 2005, LP recorded a loss of \$3.3 million related to severance charges associated with a cedar lumber facility in British Columbia.

In the second quarter of 2005, LP recorded a gain of \$1.6 million associated with the sale of a lumber facility in Michigan and a loss of \$5.0 million associated with impairment charges on assets held for sale.

# NOTE 6 INCOME TAXES

Accounting standards require that income tax expense be determined using the estimated annual effective tax rate (based upon estimated annual amounts of taxable income and expense) by income component for the year applied to year-to-date income or loss at the end of each quarter, further adjusted by any changes in reserve requirements or the impact of statutory tax rate changes, if any. Each quarter the income tax accrual is adjusted to the latest estimate and the difference from the previously accrued year-to-date balance is adjusted to the current quarter. For the six months ended June 30, 2006, the primary differences between the U.S. statutory rate of 35% and the effective rate on continuing operations relate to the company's foreign debt structure, state income taxes, and a second quarter reduction in LP's Canadian deferred tax liabilities due to an enacted decrease in the related statutory income tax rate. For the six months ended June 30, 2005, the differences between the U.S. statutory rate of 35% and the effective rate on continuing operations relate to the company's foreign debt structure and state income taxes.

The components and associated estimated effective income tax rates applied to the six-month periods ended June 30 are as follows:

	Six Months Ended June 30,			2005		
	2006			2006		
	Tax Provision	Tax Rate		Tax Provision	Tax Rate	
Continuing operations	\$ 62.6	31 %		\$ 115.5	36 %	
Discontinued operations	(0.8 )	40 %		(4.8 )	38 %	
	\$ 61.8	31 %		\$ 110.7	35 %	

# NOTE 7 - OTHER OPERATING CREDITS AND CHARGES, NET

The major components of Other operating credits and charges, net in the Condensed Consolidated Statements of Income for the quarter and six months ended June 30 are reflected in the table below and are described in the paragraphs following the table:

Dollar amounts in millions	Quarter Ended June 30, 2006	2005	Six Months Ended June 30, 2006	2005
Charges associated with corporate relocation	\$	\$ (1.5 )	\$ (0.1 )	\$ (2.1 )
Recovery on loss associated with Samoa pulp mill		0.1		0.9
Other				0.1
	\$	\$ (1.4 )	\$ (0.1 )	\$ (1.1 )

In the first quarter of 2005, LP recorded a gain of \$0.9 million associated with the recovery of a previous loss associated with the sale of the Samoa, California pulp mill and a charge of \$0.6 million associated with the relocation and consolidation of LP's corporate offices to Nashville, Tennessee.

In the second quarter of 2005, LP recorded a charge of \$1.5 million associated with the relocation and consolidation of LP's corporate offices to Nashville, Tennessee.

In the first quarter of 2006, LP recorded a charge of \$0.1 million associated with the relocation and consolidation of LP's corporate offices to Nashville, Tennessee.

#### NOTE 8 GAINS (LOSSES) ON SALE OR IMPAIRMENT OF LONG-LIVED ASSETS

The major components on Gain (loss) on sale or impairment of long-lived assets in the Condensed Consolidated Statements of Income for the quarter and six months ended June 30 are reflected in the following table:

Dollar amounts in millions	Quarter Ended June 30, 2006	2005	Six Months Ended June 30, 2006	2005
Loss on sale of long-lived assets	\$ (0.1 )	\$ (0.5 )	\$	\$ (0.3 )
Impairment reversals on long-term assets		1.2		1.2
	\$ (0.1 )	\$ 0.7	\$	\$ 0.9

In the second quarter of 2005, LP reversed \$1.2 million of the impairment recorded in the first quarter of 2004 due to management's decision to continue to retain and operate certain timber rights previously classified as discontinued operations.

#### NOTE 9 INVESTMENTS IN AND ADVANCES TO AFFILIATES

LP has investments in affiliates that are either accounted for under the equity method or the cost method based upon the specific terms of the agreement as well as advances to affiliates. The significant components of these investments and advances are as follows:

Dollar amounts in millions	June 30, 2006	December 31, 2005
Investments accounted for under the equity method	\$ 176.5	\$ 166.5
Investments accounted for under the cost method	44.5	44.5
Total	\$ 221.0	\$ 211.0

At June 30, 2006, LP's significant equity method investees and its ownership interest and principal business activity in each investee, were as follows:

	Ownership %	
U.S. GreenFiber	50%	Established to manufacture and sell cellulose insulation products
Abitibi LP	50%	Established to construct and operate jointly owned I-Joist facilities in Eastern Canada
Canfor LP	50%	Established to construct and operate a jointly owned OSB facility in British Columbia, Canada

These investments do not meet the Regulation S-X significance test requiring the inclusion of the separate investee financial statements or summarized financial information.

LP sells products and raw materials to the Abitibi-LP entity and purchases products for resale from the Abitibi-LP and Canfor-LP entities. LP eliminates profits on these sales and purchases, to the extent the inventory has not been sold through to third parties, on the basis of its 50% interest. For the quarters ended June 30, 2006 and 2005, LP sold \$8.7 million and \$5.6 million of products to Abitibi-LP and purchased \$30.1 million and \$21.6 million of I-joist from Abitibi-LP. For the six months ended June 30, 2006 and 2005, LP sold \$17.6 million and \$11.5 million of products to Abitibi-LP and purchased \$53.7 million and \$39.7 million of I-joist from Abitibi-LP. LP also purchased \$28.1 million and \$44.8 million of OSB from Canfor-LP during the quarter and six months ended June 30, 2006. LP did not purchase OSB from Canfor-LP during the quarter or six months ended June 30, 2005 as the mill was not yet operational.

#### NOTE 10 LEGAL AND ENVIRONMENTAL MATTERS

The description of certain legal and environmental matters involving LP set forth in Part II of this report under the caption "Legal Proceedings" is incorporated herein by reference.

#### NOTE 11 SELECTED SEGMENT DATA

LP operates in three segments: Oriented Strand Board (OSB); Siding; and Engineered Wood Products (EWP). LP's business units have been aggregated into these three segments based upon the similarity of economic characteristics, customers and distribution methods. LP's results of operations are summarized below for each of these segments separately as well as for the "other" category which comprises other products that are not individually significant. Segment information was prepared in accordance with the same accounting principles as those described in Note 1 of the Notes to the financial statements included in LP's Annual Report on Form 10-K for the year ended December 31, 2005.

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Dollar amounts in millions	Quarter Ended June 30,			Six Months Ended June 30,		
	2006	2005	% change	2006	2005	% change
Net sales:						
OSB	\$ 354.6	\$ 403.9	(12 )	\$ 752.3	\$ 820.1	(8 )
Siding	148.6	125.2	19	269.4	220.6	22
Engineered Wood Products	110.0	120.5	(9 )	222.4	229.8	(3 )
Other	39.5	45.6	(13 )	86.9	88.4	(2 )
Less: Intersegment sales		(3.2 )	(100 )		(5.5 )	(100 )
	\$ 652.7	\$ 692.0	(6 )	\$ 1,331.0	\$ 1,353.4	(2 )
Operating profit (loss):						
OSB	\$ 62.4	\$ 146.6	(57 )	\$ 173.3	\$ 317.9	(45 )
Siding	22.9	16.4	40	41.5	23.4	77
Engineered Wood Products	9.1	12.1	(25 )	20.3	17.7	15
Other	2.8	5.2	(46 )	8.0	10.7	(25 )
Other operating credits and charges, net		(1.4 )	100	(0.1 )	(1.1 )	91
Gain (loss) on sales of and impairment of long-lived assets	(0.1 )	0.7	(114 )		0.9	(100 )
General corporate and other expenses, net	(23.1 )	(20.2 )	(14 )	(51.5 )	(43.6 )	(18 )
Foreign currency losses	(10.6 )	(1.4 )	(657 )	(8.5 )	(2.0 )	(325 )
Investment income	24.3	16.9	44	47.3	32.4	46
Interest expense, net of capitalized interest	(14.3 )	(15.3 )	7	(27.7 )	(31.0 )	11
Income from operations before taxes	73.4	159.6	(54 )	202.6	325.3	(38 )
Provision for income taxes	18.3	55.2		62.6	115.5	
Income from continuing operations	\$ 55.1	\$ 104.4	(47 )	\$ 140.0	\$ 209.8	(33 )

NOTE 12 POTENTIAL IMPAIRMENTS

LP continues to review certain operations and investments for potential impairments. LP's management currently believes it has adequate support for the carrying value of each of these assets based upon the anticipated cash flows that result from estimates of future demand, pricing and production costs assuming certain levels of planned capital expenditures. However, should the markets for the relevant products deteriorate to levels significantly below cycle average pricing or should LP decide to invest capital in alternative projects, it is possible that impairment charges will be required.

LP also reviews from time to time possible dispositions of various assets in light of current and anticipated economic and industry conditions, its strategic plan and other relevant circumstances. Because a determination to dispose of particular assets can require management to make assumptions regarding the transaction structure of the disposition and to estimate the net sales proceeds, which may be less than previous estimates of undiscounted future net cash flows, LP may be required to record impairment charges in connection with decisions to dispose of assets.

NOTE 13 CONTINGENCY RESERVES

LP is involved in various legal proceedings incidental to LP's business and is subject to a variety of environmental and pollution control laws and regulations in all jurisdictions in which it operates. LP maintains reserves for these various contingencies as follows:

Dollar amounts in millions	June 30, 2006	December 31, 2005
Environmental reserves	\$ 8.1	\$ 10.1
Hardboard siding reserves	25.9	31.0
Other reserves	2.1	2.3
Total contingency reserves	36.1	43.4
Current portion of contingency reserves	(12.0 )	(12.0 )
Long-term portion of contingency reserves	\$ 24.1	\$ 31.4

INCENTIVE SHARE AWARDS





Hardboard Siding Reserves

LP has established reserves relating to certain liabilities associated with products manufactured that were the subject of a nationwide class action lawsuit. This settlement agreement relates to a nationwide class action suit involving hardboard siding manufactured or sold by corporations acquired by LP in 1999 and installed prior to May 15, 2000 and was approved by the applicable courts in 2000. This settlement is discussed in greater detail in the Notes to the financial statements included in LP's Annual Report on Form 10-K for the year ended December 31, 2005.

**NOTE 14 DEFINED BENEFIT PENSION PLANS**

The following table sets forth the net periodic pension cost for LP's defined benefit pension plans during the quarter and six month periods ended June 30, 2006 and 2005. The net periodic pension cost included the following components:

Dollar amounts in millions	Quarter Ended June 30,		Six Months Ended June 30,	
	2006	2005	2006	2005
Service cost	\$ 2.5	\$ 2.5	\$ 5.0	\$ 5.0
Interest cost	3.9	3.7	7.8	7.4
Expected return on plan assets	(4.6)	(3.9)	(9.2)	(7.8)
Amortization of prior service cost and transition assets	0.3	0.2	0.6	0.4
Recognized net actuarial loss	1.9	1.4	3.8	2.8
Net periodic pension cost	\$ 4.0	\$ 3.9	\$ 8.0	\$ 7.8

Through June 30, 2006, LP recognized \$8.0 million of pension expense for all of LP's defined benefit plans. LP presently anticipates recognizing an additional \$8.0 million of pension expense in the remainder of 2006 for a total of \$16.0 million.

Through June 30, 2006, LP made \$9 million of pension contributions for all of LP's defined benefit plans. LP presently anticipates contributing an additional \$9 to \$11 million to fund LP's defined benefit plans in the remainder of 2006 for a total of \$18 to \$20 million.

**NOTE 15 GUARANTEES AND INDEMNIFICATIONS**

LP is a party to contracts in which LP agrees to indemnify third parties for certain liabilities that arise out of or relate to the subject matter of the contract. In some cases, this indemnity extends to liabilities arising out of the negligence of the indemnified parties, but usually excludes any liabilities caused by gross negligence or willful misconduct of the indemnified parties. LP cannot estimate the potential amount of future payments under these agreements until events arise that would trigger the liability. See Note 20 of the Notes to the financial statements included in LP's Annual Report on Form 10-K for the year ended December 31, 2005 for further discussion of LP's guarantees and indemnifications.

Additionally, LP provides warranties on the sale of most of its products and records an accrual for estimated future claims. Such accruals are based upon historical experience and management's estimate of the level of future claims. The activity in warranty reserves for the first six months of 2006 and 2005 are summarized in the following table:

Dollar amounts in millions	June 30, 2006	June 30, 2005
Beginning balance, December 31,	\$ 32.3	\$ 22.2
Accrued to expense	2.8	2.9
Payments made	(3.6)	(3.1)
Total warranty reserves	31.5	22.0
Current portion of warranty reserves	(7.0)	(7.0)
Long-term portion of warranty reserves	\$ 24.5	\$ 15.0



The current portion of the warranty reserve is included in the caption Accounts payable and accrued liabilities and the long-term portion is included in the caption Other long-term liabilities on LP's Condensed Consolidated Balance Sheets.

NOTE 16 RECENT AND PROSPECTIVE ACCOUNTING PRONOUNCEMENTS

In June 2006, the Financial Accounting Standards Board (FASB) issued FIN 48, Accounting for Uncertainty in Income Taxes an Interpretation of FASB Statement No. 109, which clarifies the accounting for uncertain tax positions. FIN 48 provides a two-step process using a recognition threshold and measurement attribute to evaluate a tax position taken or expected to be taken in a tax return. Guidance is also provided for derecognition, classification and disclosure of uncertain tax positions. FIN 48 is effective for fiscal years beginning after December 15, 2006. LP is currently evaluating the impact of adopting FIN 48 on its financial position and results of operations.

In June 2006, the Emerging Issues Task Force (EITF) reached a consensus on Issue No. 06-3, How Taxes Collected from Customers and Remitted to Governmental Authorities Should Be Presented in the Income Statement (That Is, Gross versus Net Presentation). The scope of EITF 06-3 includes sales, use, value added and some excise taxes that are assessed by a governmental authority on specific revenue-producing transactions between a seller and customer. EITF 06-3 states that a company should disclose its accounting policy (i.e., gross or net presentation) regarding the presentation of taxes within its scope, and if significant, these disclosures should be applied retrospectively to the financial statements for all periods presented. EITF 06-3 is effective for interim and annual reporting periods beginning after December 15, 2006. LP is currently evaluating the impact of adopting EITF 06-3 on its financial statements and disclosures.

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

GENERAL

Our products are used primarily in new home construction, repair and remodeling, and manufactured housing. We also market and sell our products in light industrial and commercial construction and we have a modest export business for some of our specialty building products. Our manufacturing facilities are primarily located in the U.S. and Canada, but we also operate a facility in Chile.

To serve these markets, we operate in three segments: Oriented Strand Board (OSB), Siding, and Engineered Wood Products (EWP). OSB is the most significant segment, accounting for more than 55% of sales during the six month period ended June 30, 2006 and more than 60% of sales in the six month period ended June 30, 2005.

Our most significant product, OSB, is sold as a commodity for which sales prices fluctuate daily based on market factors over which we have little or no control. We cannot predict whether the prices of our products will remain at current levels or increase or decrease in the future. However, industry analysts believe that while demand continues to be strong for OSB, the expectation of new capacity starting up later this year coupled with lower new housing activity has led to lower pricing that will likely continue for the remainder of 2006. During the first six months of 2006, commodity OSB prices were lower compared to the same period in the prior year.

For additional factors affecting our results, refer to the Management Discussion and Analysis overview contained in our Annual Report on Form 10-K for the year ended December 31, 2005.

CRITICAL ACCOUNTING POLICIES

**LP's significant accounting policies are discussed in Note 1 of Notes to financial statements included in LP's Annual Report on Form 10-K for the year ended December 31, 2005. The discussion of each of the policies outlines the specific accounting treatment related to each of these accounting areas. While all of these are important to understand when reading our financial statements, there are certain policies that we have adopted and implemented from among acceptable alternatives that could lead to different financial results had another policy been chosen:**

*Inventory valuation.* We use the LIFO (last-in, first-out) method for some of our log inventories with the remaining inventories valued at FIFO (first-in, first-out) or average cost. Our inventories would have been approximately \$3.9 million higher if the LIFO inventories were valued at average cost as of June 30, 2006.

*Property, plant and equipment.* We principally use the units of production method of depreciation for machinery and equipment. This method amortizes the cost of machinery and equipment over the estimated units that will be produced during its estimated useful life.

#### **SIGNIFICANT ACCOUNTING ESTIMATES AND JUDGMENTS**

Throughout the preparation of the financial statements, we employ significant judgments in the application of accounting principles and methods. These judgments are primarily related to the assumptions used to arrive at various estimates. For 2006, these significant accounting estimates and judgments include:

*Legal Contingencies.* Our estimates of loss contingencies for legal proceedings are based on various judgments and assumptions regarding the potential resolution or disposition of the underlying claims and associated costs. In making judgments and assumptions regarding legal contingencies for ongoing class action settlements, we consider, among other things, discernible trends in the rate of claims asserted and related damage estimates and information obtained through consultation with statisticians and economists, including statistical analyses of potential outcomes based on experience to date and the experience of third parties who have been subject to product-related claims judged to be comparable. Due to the numerous variables associated with these judgments and assumptions, both the precision and reliability of the resulting estimates of the related loss contingencies are subject to substantial uncertainties. We regularly monitor our estimated exposure to these contingencies and, as additional information becomes known, may change our estimates significantly.

*Workers Compensation Self-Insurance Liabilities.* We are self-insured for workers compensation in most U.S. states. The liability recorded in our financial statements for self-insured workers compensation claims is based on the estimates of a third-party administrator of the future liability based on the specific facts and circumstances of each specific claim at any point in time. We do not use actuarial data from our past workers compensation claims history or general industry experience to project the growth of workers compensation claims over time. Had we done so, our workers compensation liabilities might have been higher than the amount we currently have recorded, although we cannot presently estimate by how much. During 2006, we have hired an actuary to begin a review of these claims.

*Environmental Contingencies.* Our estimates of loss contingencies for environmental matters are based on various judgments and assumptions. These estimates typically reflect judgments and assumptions relating to the probable nature, magnitude and timing of required investigation, remediation and/or monitoring activities and the probable cost of these activities, and in some cases reflect judgments and assumptions relating to the obligation or willingness and ability of third parties to bear a proportionate or allocated share of the cost of these activities, including third parties who purchased assets from us subject to environmental liabilities. We consider the ability of third parties to pay their apportioned cost when developing our estimates. In making these judgments and assumptions related to the development of our loss contingencies, we consider, among other things, the activity to date at particular sites, information obtained through consultation with applicable regulatory authorities and third-party consultants and contractors and our historical experience at other sites that are judged to be comparable. Due to the numerous variables associated with these judgments and assumptions, and the effects of changes in governmental regulation and environmental technologies, both the precision and reliability of the resulting estimates of the related contingencies are subject to substantial uncertainties. We regularly monitor our estimated exposure to environmental loss contingencies and, as additional information becomes known, may change our estimates significantly. At June 30, 2006, we excluded from our estimates approximately \$1.6 million of potential environmental liabilities that we estimate will be allocated to third parties pursuant to existing and anticipated future cost sharing arrangements.

*Impairment of Long-Lived Assets.* We review the long-lived assets held and used by us (primarily property, plant and equipment and timber and timberlands) for impairment when events or changes in circumstances indicate that the carrying amount of assets may not be recoverable. Identifying these events and changes in circumstances, and assessing their impact on the appropriate valuation of the affected assets under accounting principles generally accepted in the U.S., requires us to make judgments, assumptions and estimates. In general, on assets held and used, impairments are recognized when the book values exceed our estimate of the undiscounted future net cash flows associated with the affected assets. The key assumptions in estimating these cash flows include future production volumes and pricing of commodity or specialty products and future estimates of expenses to be incurred. Our assumptions regarding pricing are based upon the average pricing over the commodity cycle (generally five years) due to the inherent volatility of commodity product pricing. These prices are estimated from information gathered from industry research firms, research reports published by investment analysts and other published forecasts. Our estimates of expenses are based upon our long-range internal planning models and our expectation that we will continue to reduce product costs that will offset inflationary impacts.

When impairment is indicated, the book values of the assets to be held and used are written down to their estimated fair value, which is generally based upon discounted future cash flows. Assets to be disposed of are written down to their estimated fair value, less estimated selling costs. Consequently, a determination to dispose of particular assets can require us to estimate the net sales proceeds expected to be realized upon such disposition, which may be less than the estimated undiscounted future net cash flows associated with such assets prior to such determination, and thus require an impairment charge. In situations where we have experience in selling assets of a similar nature, we may estimate net sales proceeds on the basis of that experience. In other situations, we hire independent appraisers to estimate net sales proceeds. Due to the numerous variables associated with our judgments and assumptions relating to the valuation of assets in these circumstances, and the effects of changes in circumstances affecting these valuations, both the precision and reliability of the resulting estimates of the related impairment charges are subject to substantial uncertainties and, as additional information becomes known, we may change our estimates significantly.

*Income Taxes.* The determination of the provision for income taxes, and the resulting current and deferred tax assets and

liabilities, involves significant management judgment, and is based upon information and estimates available to management at the time of such determination. The final income tax liability to any taxing jurisdiction with respect to any calendar year will ultimately be determined long after our financial statements have been published for that

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year. We maintain reserves for known estimated tax exposures in federal, state and international jurisdictions; however, actual results may differ materially from our estimates.

Judgment is also applied in determining whether deferred tax assets will be realized in full or in part. When we consider it to be more likely than not that all or some portion of a deferred tax asset will not be realized, a valuation allowance is established for the amount of the deferred tax asset that is estimated not to be realizable. As of June 30, 2006, we had established valuation allowances against certain deferred tax assets, primarily related to foreign tax credit carryovers, state net operating loss and credit carryovers and foreign capital loss carryovers. We have not established valuation allowances against other deferred tax assets based upon expected future taxable income and/or tax strategies planned to mitigate the risk of impairment of these assets. Accordingly, changes in facts or circumstances affecting the likelihood of realizing a deferred tax asset could result in the need to record additional valuation allowances.

*Goodwill.* Goodwill and other intangible assets that are deemed to have an indefinite life are no longer amortized. However, these indefinite life assets are tested for impairment on an annual basis, and otherwise when indicators of impairment are determined to exist, by applying a fair value based test. The process of evaluating the potential impairment of goodwill is highly subjective and requires significant judgments at many points during the analysis. In testing for potential impairment, the estimated fair value of the reporting unit, as determined based upon cash flow forecasts, is compared to the book value of the reporting unit. The key assumptions in estimating these cash flows include future production volumes and pricing of commodity products and future estimates of expenses to be incurred. Our assumptions regarding pricing are based upon the average pricing over the commodity cycle (generally five years) due to the inherent volatility of commodity product pricing. These prices are estimated from information gathered from industry research firms, research reports published by investment analysts and other published forecasts. Our estimates of expenses are based upon our long-range internal planning models and our expectation that we will reduce product costs that will offset inflationary impacts.

Due to the numerous variables associated with our judgments and assumptions relating to the valuation of assets in these circumstances, and the effects of changes in circumstances affecting these valuations, both the precision and reliability of the resulting estimates of the related impairment charges, if any, are subject to substantial uncertainties. Consequently, as additional information becomes known, we may change our estimates significantly.

*Pension Plans.* Most of our U.S. employees and some of our Canadian employees participate in defined benefit pension plans sponsored by LP. We account for the consequences of our sponsorship of these plans in accordance with accounting principles generally accepted in the U.S., which require us to make actuarial assumptions that are used to calculate the related assets, liabilities and expenses recorded in our financial statements. While we believe we have a reasonable basis for these assumptions, which include assumptions regarding long-term rates of return on plan assets, life expectancies, rates of increase in salary levels, rates at which future values should be discounted to determine present values and other matters, the amounts of our pension related assets, liabilities and expenses recorded in our financial statements would differ if we used other assumptions. See further discussion related to pension plans below under the heading *Defined Benefit Pension Plans* and in Note 13 of the Notes to the financial statements included in item 8 of our Annual Report on Form 10-K for the year ended December 31, 2005.

## **RESULTS OF OPERATIONS**

Our net income for the second quarter of 2006 was \$55 million, or \$0.52 per diluted share, on sales of \$653 million, compared to the second quarter of 2005 net income of \$100 million, or \$0.90 per diluted share, on sales of \$692 million. For the second quarter of 2006, income from continuing operations was \$55 million, or \$0.52 per diluted share, compared to income from continuing operations of \$104 million, or \$0.94 per diluted share, for the second quarter of 2005.

Our net income for the six months ended June 30, 2006 was \$139 million, or \$1.31 per diluted share, on sales of \$1.33 billion, compared to the six months ended June 30, 2005 net income of \$202 million, or \$1.82 per diluted share, on sales of \$1.35 billion. For the six months ended June 30, 2006, income from continuing operations was \$140 million, or \$1.32 per diluted share, compared to income from continuing operations of \$210 million, or \$1.89 per diluted share, for the six months ended June 30, 2005.

Our results of operations for each of our segments are discussed below as well as for the *other* category, which



comprises products that are not individually significant.

**OSB**

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Our OSB segment manufactures and distributes commodity and value-added OSB structural panels.

Segment sales, profits and depreciation, amortization and cost of timber harvested for this segment are as follows:

	Quarter Ended June 30,			Six Months Ended June 30,			
	2006	2005	Change	2006	2005	Change	
Net sales	\$ 355	\$ 404	-12	% \$ 752	\$ 820	-8	%
Operating profits	\$ 62	\$ 147	-57	% \$ 173	\$ 318	-45	%
Depreciation, amortization and cost of timber harvested	\$ 21	\$ 22		\$ 43	\$ 44		

Percent changes in average sales prices and unit shipments for the quarter and six months ended June 30, 2006 compared to the quarter and six months ended June 30, 2005 are as follows:

	Quarter Ended June 30, 2006 versus 2005			Six Months Ended June 30, 2006 versus 2005			
	Average Net Selling Price	Unit Shipments		Average Net Selling Price	Unit Shipments		
Commodity OSB	(17	)%	7	% (16	)%	9	%

OSB prices declined for the second quarter and the first six months of 2006 compared to the corresponding periods of 2005 due to regional weakening of housing demand coupled with increased industry capacity in OSB. The reduction in selling price accounted for a decrease in net sales and operating profits of approximately \$65 million for the quarter and \$124 million for the first six months. The increase in sales volume was driven largely by higher production and improved yields at our existing manufacturing plants and start-up volumes from our Peace Valley joint venture with Canfor Corporation, for which we serve as the North American distributor of this production.

Compared to the second quarter and first six months of 2005, the primary factor, along with the reduced sales price, for decreased operating profits was the increase in our Canadian denominated manufacturing costs, a portion of the costs associated with the startup of our JV OSB mill and minor increases in petroleum based raw materials. The Canadian dollar has strengthened significantly since the first half of 2005, which causes our Canadian production costs stated in U.S. dollars to increase.

### SIDING

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Our siding segment produces and markets wood-based siding and related accessories and interior hardboard products, together with commodity OSB products from one mill not yet fully converted to siding.

Segment sales, profits and depreciation, amortization and cost of timber harvested for this segment are as follows:

	Quarter Ended June 30,				Six Months Ended June 30,			
	2006	2005	Change		2006	2005	Change	
Net sales	\$ 149	\$ 125	19	%	\$ 269	\$ 221	22	%
Operating profits	\$ 23	\$ 16	44	%	\$ 42	\$ 24	75	%
Depreciation, amortization and cost of timber harvested	\$ 5	\$ 4			\$ 10	\$ 8		

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Sales in this segment by product line are as follows:

	Quarter Ended June 30,				Six Months Ended June 30,			
	2006	2005	Change		2006	2005	Change	
OSB-based siding products	\$ 91	\$ 77	18	%	\$ 154	\$ 130	18	%
Commodity OSB products	14	3	367	%	31	5	520	%
Hardboard products	44	45	(3)	)%	84	86	(2)	)%
Total	\$ 149	\$ 125	19	%	\$ 269	\$ 221	22	%

Percent changes in average sales prices and unit shipments for the quarter and six month period ended June 30, 2006 compared to the quarter and six month period ended June 30, 2005 are as follows:

	Quarter Ended June 30, 2006 versus 2005				Six Months Ended June 30, 2006 versus 2005			
	Average Net Selling Price		Unit Shipments		Average Net Selling Price		Unit Shipments	
OSB-based siding products	5	%	12	%	7	%	12	%
Commodity OSB	(14	)%	364	%	(16	)%	362	%
Hardboard products	6	%	(7	)%	8	%	(8	)%

For the second quarter and first six months of 2006 compared to the corresponding periods in the prior year, sales volume increased in our OSB-based siding product line as well as for commodity OSB produced at one of our siding mills. Increases in our OSB-based siding product line were a result of market share gains as well as continued development of our siding trim business. The increase in commodity OSB is related to our transfer, as of January 1, 2006, of our siding production at our Silsbee, Texas mill to one of two lines at our Hayward, Wisconsin OSB facility. Currently, the Hayward mill continues to produce commodity OSB on one of its two production lines. In our hardboard product line, sales volume declined and sales prices increased due to a change in product mix that included more siding and less industrial board.

Overall, improvements in operating results for our siding segment for the second quarter and first six month of 2006 compared to the same periods of 2005 were primarily due to increased sales volumes and prices in our OSB-based siding products and improved operating performance due to the transfer of siding production to our more efficient Hayward facility discussed above. These improvements were partially offset by increases in energy and resin costs.

## ENGINEERED WOOD PRODUCTS

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Our engineered wood products (EWP) segment manufactures and distributes laminated veneer lumber (LVL), I-Joists and other related products.

Segment sales, profits and depreciation, amortization and cost of timber harvested for this segment are as follows:

	Quarter Ended June 30,			Six Months Ended June 30,			
	2006	2005	Change	2006	2005	Change	
Net sales	\$ 110	\$ 121	(9 )%	\$ 222	\$ 230	(3 )%	
Operating profits	\$ 9	\$ 12	(26 )%	\$ 20	\$ 18	13 %	
Depreciation, amortization and cost of timber harvested	\$ 3	\$ 3		\$ 7	\$7		

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Sales in this segment by product line are as follows:

	Quarter Ended June 30,			Six Months Ended June 30,		
	2006	2005	Change	2006	2005	Change
LVL	\$ 48	\$ 54	(11 )%	\$ 99	\$ 102	(3 )%
I-Joist	55	57	(4 )%	103	103	
Other	7	10	(30 )%	20	25	(20 )%
Total	\$ 110	\$ 121	(9 )%	\$ 222	\$ 230	(3 )%

Percent changes in average sales prices and unit shipments for the quarter and six months ended June 30, 2006 compared to the quarter and six months ended June 30, 2005 are as follows:

	Quarter Ended June 30, 2006 versus 2005		Six Months Ended June 30, 2006 versus 2005	
	Average Net Selling Price	Unit Shipments	Average Net Selling Price	Unit Shipments
LVL	(6 )%	(2 )%	(2 )%	(2 )%
I-Joist	(1 )%	(10 )%	(3 )%	(7 )%

During both the second quarter and first six months of 2006, we saw reductions in sales volumes in both LVL and I-Joist. These declines are attributed to regional slowdown in the housing market as well as weather related issues especially on the West Coast due to extended rain and flooding. For the quarter, net average selling prices declined slightly as we began to see sporadic price pressure. For the six month period ended June 30, 2006 compared to the same period of 2005, average net selling prices were higher due to several price increases implemented in the latter half of 2005 that remained in effect in 2006. Our focus continues to be on reductions in conversion costs, better geographic manufacturing and distribution, and maintaining key customer relationships. Included in this segment is a plywood mill, which primarily produces plywood as a by-product from the LVL production process.

The results of operations of our EWP segment for the second quarter of 2006 declined compared to the second quarter of 2005 primarily due to reductions in sales volumes and reductions in margin as we sold more of our I-Joist from production at our joint venture mills for which we share profits with our partner. The results of operations of our EWP segment for the first six months of 2006 increased compared to the same period in 2005 primarily due to higher sales prices and some reductions in raw material costs (primarily OSB and lumber) which were partially offset by increases in conversion costs and the negative affect of the higher Canadian dollar exchange rate.

## OTHER PRODUCTS



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Our other products category includes our moulding business, composite decking business, Chilean operations and our joint venture to produce cellulose insulation. Additionally, this category includes our remaining timber and timberlands and other minor products, services and operations closed prior to January 1, 2002.

Segment sales, profits and depreciation, amortization and cost of timber harvested for this category are as follows:

<b>Quarter Ended June 30,</b>	<b>Quarter Ended June 30,</b>	<b>Six Months Ended June 30,</b>
<b>2006</b>	<b>2005</b>	<b>Change</b>