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

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**FORM 10-Q**

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- QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended March 31, 2011

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: 333-130353-04

**Pregis Holding II Corporation**

(Exact name of registrant as specified in its charter)

**Delaware**

(State or other jurisdiction of  
Incorporation or Organization)

**20-3321581**

(I.R.S. Employer Identification No.)

**1650 Lake Cook Road, Deerfield, IL**  
(Address of principal executive offices)

**60015**  
(Zip Code)

Registrant's telephone number, including area code: **(847) 597-2200**

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

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

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

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

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

There were 149,0035 shares of the registrant's common stock, par value \$0.01 per share, issued and outstanding as of March 31, 2011.

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**PREGIS HOLDING II CORPORATION**  
**QUARTERLY REPORT ON FORM 10-Q**  
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**Item 1. Financial Statements**

**Pregis Holding II Corporation**  
**Consolidated Balance Sheets**  
*(dollars in thousands, except share and per share data)*

	<u>March 31, 2011</u>	<u>December 31, 2010</u>
	<u>(Unaudited)</u>	
<b>Assets</b>		
Current assets		
Cash and cash equivalents	\$ 31,066	\$ 47,845
Accounts receivable		
Trade, net of allowances of \$8,034 and \$7,513 respectively	143,026	118,836
Other	9,093	18,573
Inventories, net	103,926	88,975
Deferred income taxes	3,777	3,699
Due from Pactiv	1,133	1,161
Prepayments and other current assets	<u>10,344</u>	<u>9,131</u>
Total current assets	302,365	288,220
Property, plant and equipment, net	202,764	198,260
Other assets		
Goodwill	141,213	139,795
Intangible assets, net	53,132	53,642
Deferred financing costs, net	5,329	4,816
Due from Pactiv, long-term	8,426	8,168
Pension and related assets	12,313	11,848
Restricted Cash	3,502	3,501
Other	<u>437</u>	<u>448</u>
Total other assets	224,352	222,218
<b>Total assets</b>	<u>\$ 729,481</u>	<u>\$ 708,698</u>
<b>Liabilities and stockholder's equity</b>		
Current liabilities		
Current portion of long-term debt	\$ 4,134	\$ 46,363
Accounts payable	111,552	101,266
Accrued income taxes	4,946	2,971
Accrued payroll and benefits	17,589	14,626
Accrued interest	12,524	7,654
Other	<u>20,552</u>	<u>20,903</u>
Total current liabilities	171,297	193,783
Long-term debt	501,500	442,908
Deferred income taxes	15,100	16,029
Long-term income tax liabilities	4,177	5,732
Pension and related liabilities	4,311	4,149
Other	17,725	19,566
<b>Stockholder's equity:</b>		
Common stock — \$0.01 par value; 1,000 shares authorized, 149.0035 shares issued and outstanding at March 31, 2011 and December 2010	—	—
Additional paid-in capital	155,291	155,055
Accumulated deficit	(127,139)	(119,400)
Accumulated other comprehensive loss	<u>(12,781)</u>	<u>(9,124)</u>
Total stockholder's equity	15,371	26,531
<b>Total liabilities and stockholder's equity</b>	<u>\$ 729,481</u>	<u>\$ 708,698</u>

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

**Pregis Holding II Corporation**  
**Consolidated Statements of Operations**  
**(Unaudited)**  
*(dollars in thousands)*

	<b>Three Months Ended March 31,</b>	
	<b>2011</b>	<b>2010</b>
<b>Net Sales</b>	\$226,998	\$210,036
<b>Operating costs and expenses:</b>		
Cost of sales, excluding depreciation and amortization	178,350	162,470
Selling, general and administrative	33,074	36,880
Depreciation and amortization	12,370	11,195
Other operating expense, net	295	647
Total operating costs and expenses	224,089	211,192
<b>Operating income (loss)</b>	2,909	(1,156)
Interest expense	13,130	12,004
Interest income	—	(36)
Foreign exchange (income) loss, net	(1,128)	1,277
<b>Loss before income taxes</b>	(9,093)	(14,401)
Income tax benefit	(1,354)	(2,193)
<b>Net loss</b>	\$ (7,739)	\$ (12,208)

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

**Pregis Holding II Corporation**  
**Consolidated Statements of Cash Flows**  
**(Unaudited)**  
*(dollars in thousands)*

	<b>Three Months Ended March 31,</b>	
	<b>2011</b>	<b>2010</b>
<b>Operating activities</b>		
Net loss	\$ (7,739)	\$(12,208)
Adjustments to reconcile net loss to cash provided by operating activities:		
Depreciation and amortization	12,370	11,195
Deferred income taxes	(1,814)	(2,873)
Unrealized foreign exchange (gain) loss	(952)	1,222
Amortization of deferred financing costs	866	880
Amortization of debt discount	809	734
Gain on disposal of property, plant and equipment	(85)	(42)
Stock compensation expense	236	664
Changes in operating assets and liabilities		
Accounts and other receivables, net	(9,434)	(4,738)
Due from Pactiv	34	(64)
Inventories, net	(11,568)	(8,661)
Prepayments and other current assets	(846)	(1,001)
Accounts payable	6,472	14,383
Accrued taxes	242	(510)
Accrued interest	4,641	4,598
Other current liabilities	3,006	(1,993)
Pension and related assets and liabilities, net	(117)	(467)
Other, net	(1,994)	840
<b>Cash provided by (used in) operating activities</b>	<b>(5,873)</b>	<b>1,959</b>
<b>Investing activities</b>		
Capital expenditures	(8,429)	(6,836)
Proceeds from sale of assets	217	94
Acquisition of business, net of cash acquired	(253)	(31,385)
Change in restricted cash	—	(3,500)
<b>Cash used in investing activities</b>	<b>(8,465)</b>	<b>(41,627)</b>
<b>Financing activities</b>		
Repayment of debt	(43,000)	—
Proceeds from ABL credit facility	40,084	
Proceeds from revolving credit facility	500	500
Deferred financing fees	(1,128)	
Other, net	2	(16)
<b>Cash provided by (used in) financing activities</b>	<b>(3,542)</b>	<b>484</b>
Effect of exchange rate changes on cash and cash equivalents	1,101	(1,787)
<b>Decrease in cash and cash equivalents</b>	<b>(16,779)</b>	<b>(40,971)</b>
Cash and cash equivalents, beginning of period	47,845	80,435
<b>Cash and cash equivalents, end of period</b>	<b>\$ 31,066</b>	<b>\$ 39,464</b>

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

**Pregis Holding II Corporation**  
**Notes to Unaudited Consolidated Financial Statements**  
*(Amounts in thousands of U.S. dollars, unless otherwise noted)*

## **1. DESCRIPTION OF THE BUSINESS AND BASIS OF PRESENTATION**

### ***Description of the Business***

Pregis Corporation (“Pregis”) is an international manufacturer, marketer and supplier of protective packaging products and specialty packaging solutions. Pregis operates through two reportable segments — Protective Packaging and Specialty Packaging.

Pregis Corporation is 100%-owned by Pregis Holding II Corporation (“Pregis Holding II” or the “Company”) which is 100%-owned by Pregis Holding I Corporation (“Pregis Holding I”). AEA Investors LP and its affiliates (the “Sponsors” or “AEA”) own approximately 98% of the issued and outstanding equity of Pregis Holding I, with the remainder held by management. AEA Investors LP is a New York-based private equity investment firm.

### ***Basis of Presentation***

The consolidated financial statements included herein have been prepared in accordance with U.S. generally accepted accounting principles for interim financial information. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States (“U.S. GAAP”) for complete financial statements. Management believes these financial statements include all normal recurring adjustments considered necessary for a fair presentation of the financial position and results of operations of the Company. The results of operations for the three months ended March 31, 2011 are not necessarily indicative of the operating results for the full year.

In February 2010 the Company acquired all of the outstanding shares of IntelliPack (see Note 14). The results of operations of IntelliPack, Inc. (“IntelliPack”) are included in the consolidated results of the Company beginning February 20, 2010.

These unaudited interim financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2010.

Separate financial statements of Pregis Corporation are not presented since the floating rate senior secured notes due April 2013 and the 12.375% senior subordinated notes due October 2013 issued by Pregis Corporation are fully and unconditionally guaranteed on a senior secured and senior subordinated basis, respectively, by Pregis Holding II and all existing domestic subsidiaries of Pregis Corporation and since Pregis Holding II has no operations or assets separate from its investment in Pregis Corporation (see Note 15).

## 2. INVENTORIES

The major components of net inventories are as follows:

	March 31, 2011	December 31, 2010
Finished goods	\$ 50,567	\$ 42,192
Work-in-process	17,441	15,014
Raw materials	33,371	29,470
Other materials and supplies	2,547	2,299
	<u>\$103,926</u>	<u>\$ 88,975</u>

Inventories at March 31, 2011 and at December 31, 2010 were stated net of reserves totaling \$2,168 and \$2,156, respectively.

## 3. GOODWILL AND OTHER INTANGIBLE ASSETS

The changes in goodwill by reportable segment for the three months ended March 31, 2011 are as follows:

Segment	December 31, 2010	Foreign Currency Translation	March 31, 2011
Protective Packaging	\$ 110,326	\$ (104)	\$110,222
Specialty Packaging	29,469	1,522	30,991
Total	<u>\$ 139,795</u>	<u>\$ 1,418</u>	<u>\$141,213</u>

The Company's other intangible assets are summarized as follows:

	Average Life (Years)	March 31, 2011		December 31, 2010	
		Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Intangible assets subject to amortization:					
Customer relationships	12	\$ 50,237	\$ 20,247	\$ 48,922	\$ 18,772
Patents	10	14,345	1,900	12,097	1,352
Non-compete agreements	2 - 5	4,934	3,446	4,902	3,319
Software	3	4,290	3,275	3,971	2,884
Land use rights and other	32	1,472	713	1,390	648
Trademarks and trade names	20	3,000	163	3,000	125
In-process research and development	10	—	—	2,200	183
Intangible assets not subject to amortization:					
Trademarks and trade names		4,598	—	4,443	—
Total		<u>\$ 82,876</u>	<u>\$ 29,744</u>	<u>\$ 80,925</u>	<u>\$ 27,283</u>

Amortization expense related to intangible assets totaled \$1,924 and \$1,189 for the three months ended March 31, 2011 and 2010, respectively.

## 4. DEBT

The Company's long-term debt consists of the following:

	<u>March 31, 2011</u>	<u>December 31, 2010</u>
ABL credit facility, due March, 2016	\$ 40,084	\$ —
Revolving Credit Facility, due October, 2011	—	42,500
Senior secured 2005 notes, due April, 2013	141,740	133,700
Senior secured 2009 notes, due April, 2013 net of discount of \$6,619 at March 31, 2011 and \$6,928 at December 31, 2010	170,556	160,197
Senior subordinated notes, due October, 2013, net of discount of \$1,174 at March 31, 2011 and \$1,272 at December 31, 2010	148,826	148,728
Foreign lines of credit	4,009	3,719
Other	419	427
Total debt	<u>505,634</u>	<u>489,271</u>
Less: short-term debt	<u>(4,134)</u>	<u>(46,363)</u>
Long-term debt	<u>\$501,500</u>	<u>\$ 442,908</u>

For the three months ended March 31, 2011 the revaluation of the Company's euro-denominated senior secured notes resulted in unrealized foreign exchange loss of \$18,090 which has been partially offset by unrealized gains of \$16,609 related to the revaluation of the Company's euro-denominated intercompany notes receivable for the three months ended March 31, 2011. For the three months ended March 31, 2010, the revaluation of the Company's euro-denominated senior secured notes resulted in unrealized foreign exchange gain of \$18,158 which has been partially offset by unrealized losses of \$16,671 related to the revaluation of the Company's euro-denominated intercompany notes receivable for the three months ended March 31, 2010. These amounts are included within foreign exchange loss, net in the Company's consolidated statements of operations.

In March 2011, Pregis Holding II and Pregis and certain of their subsidiaries entered into a \$75 million Credit Agreement with Wells Fargo Capital Finance, LLC, as agent, Wells Fargo Bank, National Association, as lender and other lenders from time to time parties thereto ("ABL credit facility"). The ABL credit facility provides for borrowings in dollars, euros and pounds sterling and consists of (1) a UK facility, under which certain UK subsidiaries of Pregis (the "UK Borrowers") may from time to time borrow up to a maximum amount of the lesser of the UK borrowing base and \$30 million and (2) a US facility, under which certain US subsidiaries of Pregis (the "US Borrowers" and, together with the UK Borrowers, the "Borrowers") may from time to time borrow up to a maximum amount of the lesser of the US borrowing base and \$75 million less amounts outstanding under the UK facility. The borrowing base is calculated on the basis of certain permitted over advance amounts, plus a percentage of certain eligible accounts receivable and eligible inventory, subject to reserves established by the agent from time to time. The ABL credit facility provides for the issuances of letters of credit and a swingline subfacility. The ABL credit facility also provides for future uncommitted increases of its maximum amount, not to exceed \$40 million.

The ABL credit facility matures on the earlier of March 2016 and the date that is 90 days prior to the maturity of the existing high yield notes of Pregis Corporation (as such notes may be refinanced prior to such maturity date). Advances under the ABL credit facility bear interest, at the Borrowers' option, equal to adjusted LIBOR plus an applicable margin for LIBOR loans or a base rate plus an applicable margin for

base rate loans. The applicable margin for LIBOR loans ranges from 2.5% to 3%, depending on the average quarterly excess availability of the Borrowers. The applicable margin for base rate loans is 100 basis points lower than the applicable margin for the LIBOR loans.

All obligations under the ABL credit facility are guaranteed by Pregis Holding II and certain of its direct and indirect subsidiaries (other than certain non wholly-owned and immaterial subsidiaries and certain foreign subsidiaries), with foreign guarantors guaranteeing only the obligations of the UK Borrowers. All obligations under the ABL credit facility and the guarantees of those obligations are secured, subject to certain exceptions, by a first-priority security interest in substantially all assets of Pregis Holding II, the Borrowers and the guarantors, as well as the pledge of 100% of the capital stock of the Borrowers, the guarantors and their direct subsidiaries, with the obligations of the US Borrowers being secured only by (1) a first-priority security interest in substantially all assets of Pregis Holding II, the US Borrowers and the domestic guarantors, (2) a pledge of 100% of the capital stock of the US Borrowers, the domestic guarantors and their direct domestic subsidiaries and (3) a pledge of 65% of the voting capital stock and 100% of the non-voting capital stock of the first-tier foreign subsidiaries of the US Borrowers and domestic guarantors. The security interest in the domestic collateral ranks prior to the security interest securing the Company's existing second priority floating rate notes due 2013. The lenders under the ABL credit facility have agreed to share their domestic collateral with future secured notes, if any, that refinance the existing notes, with the ABL credit facility retaining a first priority security interest in all accounts receivable, inventory and certain related assets of Pregis Holding II, the US Borrowers and the domestic guarantors and subordinating its security interest in all other domestic assets and the capital stock of the US Borrowers, domestic guarantors and their direct subsidiaries to the liens securing such new secured notes, if any.

As of March 31, 2011, borrowings under the ABL credit facility totaled \$40,084, outstanding letters of credit were \$6,750, and remaining availability was \$28,166. The Company utilized proceeds from the ABL credit facility to pay off and terminate its pre-existing \$50 million revolving credit facility. It is the current intent of the Company to hold the debt until its maturity, resulting in the debt's classification as long-term as of March 31, 2011.

Pregis's senior secured notes were issued in the principal amount of €100.0 million and €125.0 million, respectively, and bear interest at a floating rate equal to EURIBOR (as defined) plus 5.00% per year (for a total rate of 5.985% as of December 31, 2010). Interest resets quarterly and is payable quarterly on January 15, April 15, July 15 and October 15. The senior secured notes mature on April 15, 2013. The senior subordinated notes were issued in the principal amount of \$150.0 million and bear interest at the rate of 12.375% annually. Interest on the senior subordinated notes is payable semi-annually on April 15 and October 15. The senior subordinated notes mature on October 15, 2013. The senior subordinated notes were issued at a discount of 98.149% of their principal amount, resulting in an initial discount of \$2.8 million, which is being amortized using the effective interest method over the term of the notes. The senior secured notes issued in 2009 were issued at a discount of 94% of their principal amount, resulting in an initial discount of \$11.0 million, (€7.5million), which is being amortized using the effective interest method over the term of the notes. The senior secured notes and senior subordinated notes do not have required principal payments prior to maturity.

Pregis Holding II and Pregis's domestic subsidiaries have guaranteed the obligations under the senior secured notes and the senior subordinated notes on a senior secured basis and senior subordinated basis, respectively. Additionally, the senior secured notes are secured on a second priority basis by liens on all of the domestic collateral (subject to certain exceptions) securing Pregis's ABL credit facility. In the event that secured creditors exercise remedies with respect to Pregis and its guarantors' pledged assets, the proceeds of the liquidation of those assets will first be applied to repay obligations secured by the first priority liens under the ABL credit facility and any other first priority obligations.

In March 2011, the Company borrowed amounts available to its foreign subsidiaries under two local lines of credit. The first subsidiary line of credit allows for borrowings up to a certain percentage of such subsidiary's specified accounts receivable. As of March 31, 2011 amounts outstanding under this foreign line of credit totaled \$4.0 million. The second foreign line of credit allows for issuances of letters of credit only which totaled \$3.6 million as of March 31, 2011.

## 5. FAIR VALUE MEASUREMENTS

Under U.S. GAAP, certain assets and liabilities must be measured at fair value and ASC Topic 820, *Fair Value Measurements and Disclosures*, ("ASC Topic 820") details the disclosures that are required for items measured at fair value.

ASC Topic 820 establishes a three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value, as follows:

Level 1 — Quoted prices in active markets for identical assets and liabilities.

Level 2 — Observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities, quoted prices in markets that are not active, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 — Unobservable inputs in which little or no market data exists, therefore requiring an entity to develop its own assumptions.

In order to maintain its interest rate risk and to achieve a targeted ratio of variable-rate versus fixed-rate debt, the Company established an interest rate swap arrangement in the notional amount of 65 million euro from EURIBOR-based floating rates to a fixed rate over the period of October 1, 2008 to April 15, 2011. This swap arrangement was designated as a cash flow hedge and changes in the fair value of this instrument are expected to be highly effective in offsetting the fluctuations in the floating interest rate and are, therefore, being recorded in other comprehensive income until the underlying transaction is recorded. This swap arrangement was settled in March 2011.

The accounting for the cash flow impact of the swap was recorded as an adjustment to interest expense. For the three months ended March 31, 2011, the swap resulted in an increase to interest expense of \$1,654, which included additional expense of \$838 related to the termination of the swap. For the three months ended March 31, 2010, the swap resulted in an increase to interest expense of \$927.

At March 31, 2011, the Company's contingent purchase consideration relating to the IntelliPack acquisition in 2010 is recorded at fair value and is categorized as Level 3 within the fair value hierarchy. The fair value of this liability is estimated using a present value analysis as of March 31, 2011 and was \$9.4 million. This analysis considers, among other items, the financial forecasts of future operating results of the acquiree, the probability of reaching the forecast, and the associated discount rate. A rollforward of this liability from the acquisition date to the balance sheet date is as follows:

	<b>Fair Value Measurements at Reporting Date Using Significant Unobservable Inputs (Level 3)</b>
Contingent purchase consideration liability	
Fair value at acquisition date	\$ 9,700
Payments	(772)
Change in fair value (1)	672
Balance as of December 31, 2010	<u>\$ 9,600</u>
Payments	(253)
Change in fair value (1)	53
Balance as of March 31, 2011	<u><u>\$ 9,400</u></u>

(1) The adjustment to original contingent purchase consideration liability recorded was the result of using revised financial forecasts and updated fair value measurement and is included in interest expense in the statement of operations

The carrying values of other financial instruments included in current assets and current liabilities approximate fair values due to the short-term maturities of these instruments. The carrying value of amounts outstanding under the Company's senior secured credit facilities is considered to approximate fair value as interest rates vary, based on prevailing market rates. At March 31, 2011, the fair values of the Company's senior secured notes (issued in 2005), senior secured notes (issued in 2009), and senior subordinated notes were estimated to be \$137,488, \$171,860, and \$145,125 respectively, based on quoted market prices. Under ASC Topic 825, "Financial Instruments", entities are permitted to choose to measure many financial instruments and certain other items at fair value. The Company did not elect the fair value measurement option under this standard for any of its financial assets or liabilities.

## 6. PENSION PLANS

The Company sponsors three defined benefit pension plans covering the majority of its employees located in the United Kingdom and the Netherlands.

The components of net periodic pension cost related to these plans for the three months ended March 31, 2011 and 2010 are as follows:

	<b>Three Months Ended March 31,</b>	
	<b>2011</b>	<b>2010</b>
Service cost of benefits earned	\$ 588	\$ 496
Interest cost on benefit obligations	1,291	1,178
Expected return on plan assets	(1,642)	(1,596)
Amortization of unrecognized net gain	—	(10)
Net periodic pension cost	<u>\$ 237</u>	<u>\$ 68</u>

## 7. OTHER OPERATING EXPENSE, NET

A summary of the items comprising other operating expense, net is as follows:

	<u>Three Months Ended March 31,</u>	
	<u>2011</u>	<u>2010</u>
Gain on disposal of property, plant and equipment	\$ (85)	\$ (42)
Restructuring expense	486	630
Other expense, net	(106)	59
Other operating expense, net	<u>\$ 295</u>	<u>\$ 647</u>

Restructuring activities are discussed further in Note 8 below.

## 8. RESTRUCTURING ACTIVITY

In 2010, the Company incurred restructuring costs in its European operations in an effort to upgrade management and to further drive cost reductions. The Company used outside consultants to aid in this process. These efforts have continued in 2011.

Following is a reconciliation of the restructuring liability for the three months ended March 31, 2011.

<u>Segment</u>	<u>December 31,</u> <u>2010</u>	<u>Severance</u>	<u>Other</u>	<u>Cash</u> <u>Paid Out</u>	<u>Foreign Currency</u> <u>Translation</u>	<u>March 31,</u> <u>2011</u>
Protective Packaging	\$ 135	\$ 32	\$ 185	\$ (276)	\$ 3	\$ 79
Specialty Packaging	822	3	—	(430)	35	430
Corporate	—	—	266	(266)	—	—
Total	<u>\$ 957</u>	<u>\$ 35</u>	<u>\$ 451</u>	<u>\$ (972)</u>	<u>\$ 38</u>	<u>\$ 509</u>

Amounts recorded for restructuring liabilities are included in other current liabilities on the Company's consolidated balance sheets.

## 9. INCOME TAXES

The Company's effective tax rate was (14.89)% and (15.23)% for the three months ended March 31, 2011 and 2010, respectively. Reconciliation of the Company's effective tax rate to the U.S. federal statutory rate is shown in the following table:

	<b>Three Months Ended March 31,</b>	
	<b>2011</b>	<b>2010</b>
U.S. federal income tax rate	(35.00)%	(35.00)%
Changes in income tax rate resulting from:		
Valuation allowances	14.58	18.74
State and local taxes on income, net of U.S. federal income tax benefit	(1.36)	(0.63)
Foreign rate differential	0.53	0.45
Permanent differences	2.08	1.35
Other	4.28	(0.14)
Income tax benefit	<u>(14.89)%</u>	<u>(15.23)%</u>

## 10. RELATED PARTY TRANSACTIONS

The Company is party to a management agreement with its sponsors, AEA Investors LP and its affiliates, who provide various advisory and consulting services. Fees and expenses incurred under this agreement totaled \$510 for the three months ended March 31, 2011, and \$962 for the same period of 2010 which included a \$500 fee for services related to the acquisition of IntelliPack.

The Company had sales to affiliates of AEA Investors LP totaling \$1,431 for the three months ended March 31, 2011 compared to \$402 for the same period of 2010. The Company made purchases from affiliates of AEA Investors LP totaling \$5,169 for the three months ended March 31, 2011 compared to \$4,123 for the same period of 2010.

## 11. SEGMENT AND GEOGRAPHIC INFORMATION

The Company's segments are determined on the basis of its organization and internal reporting to the chief operating decision maker. The Company's segments are as follows:

**Protective Packaging** — This segment manufactures, markets, sells and distributes protective packaging products in North America and Europe. Its protective mailers, air-encapsulated bubble products, sheet foam, engineered foam, inflatable airbag systems, honeycomb products, foam-in-place, and other protective packaging products are manufactured and sold for use in cushioning, void-fill, surface-protection, containment and blocking & bracing applications.

**Specialty Packaging** — This segment provides innovative packaging solutions for food, medical, and other specialty packaging applications, primarily in Europe.

Net sales by reportable segment for the three months ended March 31, 2011 and 2010 are as follows:

	<b>Three Months Ended March 31,</b>	
	<b>2011</b>	<b>2010</b>
Protective Packaging	\$ 146,018	\$ 134,860
Specialty Packaging	80,980	75,176
	<u>\$ 226,998</u>	<u>\$ 210,036</u>

The Company evaluates performance and allocates resources to its segments based on segment EBITDA, which is calculated internally as net income before interest, taxes, depreciation, amortization, and

restructuring expense and adjusted for other non-cash charges and benefits. Segment EBITDA is a measure of segment profit or loss which is reported to the Company's chief operating decision maker for purposes of making decisions about allocating resources to the Company's segments and evaluating segment performance. In addition, segment EBITDA is included herein in conformity with ASC Topic 280, "Disclosures about Segments of an Enterprise and Related Information." Management believes that segment EBITDA provides useful information for analyzing and evaluating the underlying operating results of each segment. However, segment EBITDA should not be considered in isolation or as a substitute for net income (loss) before income taxes or other measures of financial performance prepared in accordance with generally accepted accounting principles in the United States. Additionally, the Company's computation of segment EBITDA may not be comparable to other similarly titled measures computed by other companies.

The following table presents EBITDA by reportable segment and reconciles the total segment EBITDA to loss before income taxes:

	<b>Three Months Ended March 31,</b>	
	<b>2011</b>	<b>2010</b>
<b>Segment EBITDA</b>		
Protective Packaging	\$ 12,175	\$ 10,781
Specialty Packaging	9,094	9,544
<b>Total segment EBITDA</b>	<b>21,269</b>	<b>20,325</b>
Corporate expenses	(5,092)	(9,047)
Restructuring expense	(486)	(630)
Depreciation and amortization	(12,370)	(11,195)
Interest expense	(13,130)	(12,004)
Interest income	—	36
Unrealized foreign exchange loss, net	952	(1,222)
Non-cash stock compensation	(236)	(664)
<b>Loss before income taxes</b>	<b>\$ (9,093)</b>	<b>\$ (14,401)</b>

Corporate expenses include the costs of corporate support functions, such as information technology, finance, human resources, legal and executive management which have not been allocated to the segments. Additionally, corporate expenses may include other non-recurring or non-operational activity that the chief operating decision maker excludes in assessing business unit performance. These expenses, along with depreciation and amortization, other operating income/expense and other non-operating activity such as interest expense/income, restructuring, and foreign exchange gains/losses, are not considered in the measure of the segments' operating performance, but are shown herein as reconciling items to the Company's consolidated loss before income taxes.

## 12. COMPREHENSIVE LOSS

Total comprehensive loss and its components for the three months ended March 31, 2011 and 2010 are as follows:

	Three Months Ended March 31,	
	2011	2010
Net loss	\$ (7,739)	\$ (12,208)
Other comprehensive income (loss), net of tax:		
Foreign currency translation adjustment	(4,678)	3,309
Net change in fair value of hedging instrument	1,021	394
Comprehensive loss	<u>\$ (11,396)</u>	<u>\$ (8,505)</u>

As discussed in Note 5, the Company settled the interest rate swap in March 2011. The change in fair value of the swap through the date of settlement was recorded in other comprehensive income (loss) and the amount remaining in accumulated other comprehensive income (loss) on the date of settlement was recorded as interest expense.

## 13. COMMITMENTS AND CONTINGENCIES

### Legal matters

The Company is party to legal proceedings arising from its operations. Related reserves are recorded when it is probable that liabilities exist and where reasonable estimates of such liabilities can be made. While it is not possible to predict the outcome of any of these proceedings, the Company's management, based on its assessment of the facts and circumstances now known, does not believe that any of these proceedings, individually or in the aggregate, will have a material adverse effect on the Company's financial position. The Company does not believe that, with respect to any pending legal matters, it is reasonably possible that a loss exceeding amounts already recognized may be material. However, actual outcomes may be different than expected and could have a material effect on the company's results of operations or cash flows in a particular period.

### Environmental matters

The Company is subject to a variety of environmental and pollution-control laws and regulations in all jurisdictions in which it operates. Where it is probable that related liabilities exist and where reasonable estimates of such liabilities can be made, associated reserves are established. Estimated liabilities are subject to change as additional information becomes available regarding the magnitude of possible clean-up costs, the expense and effectiveness of alternative clean-up methods, and other possible liabilities associated with such situations. The Company does not believe that, with respect to any pending environmental matters, that a loss is reasonably possible. However, actual outcomes may be different than expected and could have a material effect on the company's results of operations or cash flows in a particular period.

### Financing commitments

As of March 31, 2011, the Company also had \$6.7 million of outstanding letters of credit under the ABL credit facility. In addition, the Company also had outstanding guarantees and letters of credit issued under other financing lines with local banks totaling \$3.6 million.

## 14. ACQUISITIONS

The transaction discussed below was accounted for using the purchase method of accounting. Accordingly the purchase price was allocated to the assets acquired, liabilities assumed, and identifiable intangible assets as applicable based on their fair values at the date of acquisition. Any excess of purchase price over the fair value of net assets acquired was recorded as goodwill. The results of operations of the acquiree is included in the Company's consolidated financial statements since the date of acquisition. The goodwill related to this acquisition is not tax-deductible.

In February 2010, Pregis acquired all of the outstanding stock of IntelliPack, Inc. through one of its wholly owned subsidiaries, Pregis Management Corporation (the "IntelliPack Acquisition"). Following the acquisition, Pregis Management Corporation was subsequently renamed Pregis IntelliPack Corporation ("IntelliPack"). The initial purchase price of \$31.5 million, including certain escrowed amounts totaling \$3.5 million, was funded with cash-on-hand. In accordance with the terms of the agreement, additional consideration up to a maximum of \$11.5 million may be payable by Pregis if certain future performance targets are achieved by IntelliPack. Based on a present value analysis, the fair value of contingent purchase consideration was valued at approximately \$9.7 million on the acquisition date. The Company paid \$0.3 million as of March 31, 2011 and \$0.8 million during 2010 related to this contingency. The remaining contingent purchase consideration was revalued at approximately \$9.4 million as of March 31, 2011. The classification of the additional consideration payable as current and long-term was based on the estimated timing of future payments and the amounts are included in other current liabilities and other long-term liabilities in the consolidated balance sheet.

## 15. SUPPLEMENTAL GUARANTOR CONDENSED FINANCIAL INFORMATION

Pregis Holdings II (presented as Parent in the following schedules), through its 100%-owned subsidiary, Pregis Corporation (presented as Issuer in the following schedules), issued senior secured notes and senior subordinated notes in connection with its acquisition by AEA Investors LP and its affiliates. The senior notes are fully, unconditionally and jointly and severally guaranteed on a senior secured basis and the senior subordinated notes are fully, unconditionally and jointly and severally guaranteed on an unsecured senior subordinated basis, in each case, by Pregis Holdings II and substantially all existing and future 100%-owned domestic restricted subsidiaries of Pregis Corporation (collectively, the "Guarantors"). All other subsidiaries of Pregis Corporation, whether direct or indirect, do not guarantee the senior secured notes and senior subordinated notes (the "Non-Guarantors"). The Guarantors also unconditionally guarantee the Company's borrowings under its ABL credit facility on a senior secured basis.

Additionally, the senior secured notes are secured on a second priority basis by liens on all of the collateral (subject to certain exceptions) securing Pregis Corporation's senior secured credit facilities. In the event that secured creditors exercise remedies with respect to Pregis and its guarantors' pledged assets, the proceeds of the liquidation of those assets will first be applied to repay obligations secured by the first priority liens under the ABL credit facility and any other first priority obligations.

The following condensed consolidating financial statements present the results of operations, financial position and cash flows of (1) the Parent, (2) the Issuer, (3) the Guarantors, (4) the Non-Guarantors, and (5) eliminations to arrive at the information for Pregis Holding II on a consolidated basis. Separate financial statements and other disclosures concerning the Guarantors are not presented because management does not believe such information is material to investors. Therefore, each of the Guarantors is combined in the presentation below.

**Pregis Holding II Corporation**  
**Condensed Consolidating Balance Sheet**  
**March 31, 2011**

	<u>Parent</u>	<u>Issuer</u>	<u>Guarantor Subsidiaries</u>	<u>Non- Guarantor Subsidiaries</u>	<u>Eliminations</u>	<u>Consolidated</u>
<b>Assets</b>						
<b>Current assets</b>						
Cash and cash equivalents	\$ —	\$ 5,272	\$ 510	\$ 25,284	\$ —	\$ 31,066
Accounts receivable						
Trade, net of allowances	—	—	34,929	108,097	—	143,026
Affiliates	—	85,448	120,440	(2,669)	(203,219)	—
Other	—	—	6	9,087	—	9,093
Inventories, net	—	—	23,152	80,774	—	103,926
Deferred income taxes	—	134	3,070	573	—	3,777
Due from Pactiv	—	56	—	1,077	—	1,133
Prepayments and other current assets	—	4,534	1,142	4,668	—	10,344
Total current assets	—	95,444	183,249	226,891	(203,219)	302,365
Investment in subsidiaries / intercompany balances	15,371	488,213	—	—	(503,584)	—
Property, plant and equipment, net	—	910	55,796	146,058	—	202,764
<b>Other assets</b>						
Goodwill	—	—	100,684	40,529	—	141,213
Intangible assets, net	—	—	34,250	18,882	—	53,132
Restricted cash	—	3,502	—	—	—	3,502
Other	—	5,349	3,527	17,629	—	26,505
Total other assets	—	8,851	138,461	77,040	—	224,352
<b>Total assets</b>	<u>\$15,371</u>	<u>\$593,418</u>	<u>\$ 377,506</u>	<u>\$ 449,989</u>	<u>\$ (706,803)</u>	<u>\$ 729,481</u>
<b>Liabilities and stockholder's equity</b>						
<b>Current liabilities</b>						
Current portion of long-term debt	\$ —	\$ —	\$ —	\$ 4,134	\$ —	\$ 4,134
Accounts payable	—	5,764	19,291	86,497	—	111,552
Accounts payable, affiliate	—	79,352	93,888	29,834	(203,074)	—
Accrued income taxes	—	(1,596)	1,678	4,864	—	4,946
Accrued payroll and benefits	—	2,069	4,175	11,345	—	17,589
Accrued interest	—	12,524	—	—	—	12,524
Other	—	4,472	5,748	10,332	—	20,552
Total current liabilities	—	102,585	124,780	147,006	(203,074)	171,297
Long-term debt	—	481,205	—	20,295	—	501,500
Intercompany balances	—	—	77,385	292,814	(370,199)	—
Deferred income taxes	—	(13,581)	24,625	4,056	—	15,100
Other long-term liabilities	—	7,838	7,516	10,859	—	26,213
Total Stockholder's equity	15,371	15,371	143,200	(25,041)	(133,530)	15,371
<b>Total liabilities and stockholder's equity</b>	<u>\$15,371</u>	<u>\$593,418</u>	<u>\$ 377,506</u>	<u>\$ 449,989</u>	<u>\$ (706,803)</u>	<u>\$ 729,481</u>

**Pregis Holding II Corporation**  
**Condensed Consolidating Balance Sheet**  
**December 31, 2010**

	Parent	Issuer	Guarantor Subsidiaries	Non- Guarantor Subsidiaries	Eliminations	Consolidated
<b>Assets</b>						
<b>Current assets</b>						
Cash and cash equivalents	\$ —	\$ 19,019	\$ 763	\$ 28,063	\$ —	\$ 47,845
Accounts receivable						
Trade, net of allowances	—	—	33,165	85,671	—	118,836
Affiliates	—	67,201	90,017	4,334	(161,552)	—
Other	—	—	9	18,564	—	18,573
Inventories, net	—	—	23,521	65,454	—	88,975
Deferred income taxes	—	134	3,070	495	—	3,699
Due from Pactiv	—	56	—	1,105	—	1,161
Prepayments and other current assets	—	4,269	1,488	3,374	—	9,131
Total current assets	—	90,679	152,033	207,060	(161,552)	288,220
Investment in subsidiaries / intercompany balances	26,531	475,692	—	—	(502,223)	—
Property, plant and equipment, net	—	1,042	55,764	141,454	—	198,260
<b>Other assets</b>						
Goodwill	—	—	100,684	39,111	—	139,795
Intangible assets, net	—	—	35,121	18,521	—	53,642
Restricted cash	—	3,501	—	—	—	3,501
Other	—	4,836	3,527	16,917	—	25,280
Total other assets	—	8,337	139,332	74,549	—	222,218
<b>Total assets</b>	<b><u>\$26,531</u></b>	<b><u>\$575,750</u></b>	<b><u>\$ 347,129</u></b>	<b><u>\$ 423,063</u></b>	<b><u>\$ (663,775)</u></b>	<b><u>\$ 708,698</u></b>
<b>Liabilities and stockholder's equity</b>						
<b>Current liabilities</b>						
Current portion of long-term debt	\$ —	\$ 42,500	\$ —	\$ 3,863	\$ —	\$ 46,363
Accounts payable	—	5,243	22,537	73,486	—	101,266
Accounts payable, affiliate	—	50,104	62,896	48,415	(161,415)	—
Accrued income taxes	—	(1,597)	1,665	2,903	—	2,971
Accrued payroll and benefits	—	446	4,456	9,724	—	14,626
Accrued interest	—	7,619	—	35	—	7,654
Other	—	5,136	6,137	9,630	—	20,903
Total current liabilities	—	109,451	97,691	148,056	(161,415)	193,783
Long-term debt	—	442,625	—	283	—	442,908
Intercompany balances	—	—	77,384	276,200	(353,584)	—
Deferred income taxes	—	(12,373)	24,625	3,777	—	16,029
Other long-term liabilities	—	9,516	7,694	12,237	—	29,447
Total Stockholder's equity	26,531	26,531	139,735	(17,490)	(148,776)	26,531
<b>Total liabilities and stockholder's equity</b>	<b><u>\$26,531</u></b>	<b><u>\$575,750</u></b>	<b><u>\$ 347,129</u></b>	<b><u>\$ 423,063</u></b>	<b><u>\$ (663,775)</u></b>	<b><u>\$ 708,698</u></b>

**Pregis Holding II Corporation**  
**Condensed Consolidating Statement of Operations**  
**For the Three Months Ended March 31, 2011**  
**(Unaudited)**

	<u>Parent</u>	<u>Issuer</u>	<u>Guarantor Subsidiaries</u>	<u>Non- Guarantor Subsidiaries</u>	<u>Eliminations</u>	<u>Consolidated</u>
<b>Net Sales</b>	\$ —	\$ —	\$ 84,005	\$ 145,732	\$ (2,739)	\$ 226,998
<b>Operating costs and expenses:</b>						
Cost of sales, excluding depreciation and amortization	—	—	62,876	118,213	(2,739)	178,350
Selling, general and administrative	—	5,327	10,795	16,952	—	33,074
Depreciation and amortization	—	132	4,462	7,776	—	12,370
Other operating expense, net	—	257	(6)	44	—	295
<b>Total operating costs and expenses</b>	<b>—</b>	<b>5,716</b>	<b>78,127</b>	<b>142,985</b>	<b>(2,739)</b>	<b>224,089</b>
<b>Operating income (loss)</b>	<b>—</b>	<b>(5,716)</b>	<b>5,878</b>	<b>2,747</b>	<b>—</b>	<b>2,909</b>
Interest expense	—	5,237	2,394	5,499	—	13,130
Foreign exchange loss, net	—	(945)	—	(183)	—	(1,128)
Equity in loss of subsidiaries	7,739	(594)	—	—	(7,145)	—
<b>Income (loss) before income taxes</b>	<b>(7,739)</b>	<b>(9,414)</b>	<b>3,484</b>	<b>(2,569)</b>	<b>7,145</b>	<b>(9,093)</b>
Income tax expense (benefit)	—	(1,675)	20	301	—	(1,354)
<b>Net income (loss)</b>	<b><u>\$(7,739)</u></b>	<b><u>\$(7,739)</u></b>	<b><u>\$ 3,464</u></b>	<b><u>\$ (2,870)</u></b>	<b><u>\$ 7,145</u></b>	<b><u>\$ (7,739)</u></b>

**Pregis Holding II Corporation**  
**Condensed Consolidating Statement of Operations**  
**For the Three Months Ended March 31, 2010**  
**(Unaudited)**

	<u>Parent</u>	<u>Issuer</u>	<u>Guarantor Subsidiaries</u>	<u>Non- Guarantor Subsidiaries</u>	<u>Eliminations</u>	<u>Consolidated</u>
<b>Net Sales</b>	\$ —	\$ —	\$ 75,459	\$ 137,227	\$ (2,650)	\$ 210,036
<b>Operating costs and expenses:</b>						
Cost of sales, excluding depreciation and amortization	—	—	56,215	108,905	(2,650)	162,470
Selling, general and administrative	—	9,481	9,953	17,446	—	36,880
Depreciation and amortization	—	129	3,816	7,250	—	11,195
Other operating expense, net	—	210	(9)	446	—	647
<b>Total operating costs and expenses</b>	<b>—</b>	<b>9,820</b>	<b>69,975</b>	<b>134,047</b>	<b>(2,650)</b>	<b>211,192</b>
<b>Operating income (loss)</b>	<b>—</b>	<b>(9,820)</b>	<b>5,484</b>	<b>3,180</b>	<b>—</b>	<b>(1,156)</b>
Interest expense	—	3,381	3,266	5,357	—	12,004
Interest income	—	(5)	—	(31)	—	(36)
Foreign exchange loss, net	—	1,124	—	153	—	1,277
Equity in loss of subsidiaries	12,208	1,655	—	—	(13,863)	—
<b>Income (loss) before income taxes</b>	<b>(12,208)</b>	<b>(15,975)</b>	<b>2,218</b>	<b>(2,299)</b>	<b>13,863</b>	<b>(14,401)</b>
Income tax expense (benefit)	—	(3,767)	935	639	—	(2,193)
<b>Net income (loss)</b>	<b><u>\$(12,208)</u></b>	<b><u>\$(12,208)</u></b>	<b><u>\$ 1,283</u></b>	<b><u>\$ (2,938)</u></b>	<b><u>\$ 13,863</u></b>	<b><u>\$ (12,208)</u></b>

**Pregis Holding II Corporation**  
**Condensed Consolidating Statement of Cash Flows**  
**For the Three Months Ended March 31, 2011**  
**(Unaudited)**

	<u>Parent</u>	<u>Issuer</u>	<u>Guarantor Subsidiaries</u>	<u>Non- Guarantor Subsidiaries</u>	<u>Eliminations</u>	<u>Consolidated</u>
<b>Operating activities</b>						
Net income (loss)	\$(7,739)	\$ (7,739)	\$ 3,464	\$ (2,870)	\$ 7,145	\$ (7,739)
Non-cash adjustments	7,739	(1,136)	4,442	7,530	(7,145)	11,430
Changes in operating assets and liabilities, net of effects of acquisitions	—	18,925	(4,224)	(24,265)	—	(9,564)
<b>Cash provided by (used in) operating activities</b>	<u>—</u>	<u>10,050</u>	<u>3,682</u>	<u>(19,605)</u>	<u>—</u>	<u>(5,873)</u>
<b>Investing activities</b>						
Capital expenditures	—	—	(3,961)	(4,468)	—	(8,429)
Proceeds from sale of assets	—	—	26	191	—	217
Acquisition of business, net of cash acquired	—	(253)	—	—	—	(253)
Change in restricted cash	—	—	—	—	—	—
<b>Cash used in investing activities</b>	<u>—</u>	<u>(253)</u>	<u>(3,935)</u>	<u>(4,277)</u>	<u>—</u>	<u>(8,465)</u>
<b>Financing activities</b>						
Proceeds from ABL credit facility	—	20,084	—	20,000	—	40,084
Proceeds from revolving credit facility	—	500	—	—	—	500
Repayment of long-term debt	—	(43,000)	—	—	—	(43,000)
Deferred financing fees	—	(1,128)	—	—	—	(1,128)
Other, net	—	—	—	2	—	2
<b>Cash provided by (used in) financing activities</b>	<u>—</u>	<u>(23,544)</u>	<u>—</u>	<u>20,002</u>	<u>—</u>	<u>(3,542)</u>
Effect of exchange rate changes on cash and cash equivalents	—	—	—	1,101	—	1,101
Decrease in cash and cash equivalents	—	(13,747)	(253)	(2,779)	—	(16,779)
Cash and cash equivalents, beginning of period	—	19,019	763	28,063	—	47,845
Cash and cash equivalents, end of period	<u>\$ —</u>	<u>\$ 5,272</u>	<u>\$ 510</u>	<u>\$ 25,284</u>	<u>\$ —</u>	<u>\$ 31,066</u>

**Pregis Holding II Corporation**  
**Condensed Consolidating Statement of Cash Flows**  
**For the Three Months Ended March 31, 2010**  
**(Unaudited)**

	<u>Parent</u>	<u>Issuer</u>	<u>Guarantor Subsidiaries</u>	<u>Non- Guarantor Subsidiaries</u>	<u>Eliminations</u>	<u>Consolidated</u>
<b>Operating activities</b>						
Net income (loss)	\$(12,208)	\$(12,208)	\$ 1,283	\$ (2,938)	\$ 13,863	\$ (12,208)
Non-cash adjustments	12,208	749	4,745	7,207	(13,863)	11,046
Changes in operating assets and liabilities, net of effects of acquisitions	—	5,003	1,210	(3,092)	—	3,121
<b>Cash provided by (used in) operating activities</b>	<u>—</u>	<u>(6,456)</u>	<u>7,238</u>	<u>1,177</u>	<u>—</u>	<u>1,959</u>
<b>Investing activities</b>						
Capital expenditures	—	(170)	(2,847)	(3,819)	—	(6,836)
Proceeds from sale of assets	—	—	—	94	—	94
Acquisition of business, net of cash acquired	—	(31,500)	115	—	—	(31,385)
Change in restricted cash	—	(3,500)	—	—	—	(3,500)
<b>Cash used in investing activities</b>	<u>—</u>	<u>(35,170)</u>	<u>(2,732)</u>	<u>(3,725)</u>	<u>—</u>	<u>(41,627)</u>
<b>Financing activities</b>						
Intercompany activity	—	4,008	(4,008)	—	—	—
Proceeds from issuance of long-term debt	—	500	—	—	—	500
Other, net	—	—	—	(16)	—	(16)
<b>Cash provided by (used in) financing activities</b>	<u>—</u>	<u>4,508</u>	<u>(4,008)</u>	<u>(16)</u>	<u>—</u>	<u>484</u>
Effect of exchange rate changes on cash and cash equivalents	—	(105)	—	(1,682)	—	(1,787)
Increase (decrease) in cash and cash equivalents	—	(37,223)	498	(4,246)	—	(40,971)
Cash and cash equivalents, beginning of period	—	40,883	—	39,552	—	80,435
Cash and cash equivalents, end of period	<u>\$ —</u>	<u>\$ 3,660</u>	<u>\$ 498</u>	<u>\$ 35,306</u>	<u>\$ —</u>	<u>\$ 39,464</u>

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

*This following discussion and analysis should be read in conjunction with the consolidated financial statements and notes appearing elsewhere in this report and the Company's audited financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2010.*

### Cautionary Note Regarding Forward-Looking Statements

This report contains forward-looking statements within the meaning of Section 27A of the Securities Act and Section 21E in the Securities Exchange Act of 1934, as amended (the "Exchange Act"). You can generally identify forward-looking statements by our use of forward-looking terminology such as "anticipate," "believe," "continue," "could," "estimate," "expect," "intend," "may," "might," "plan," "potential," "predict," "seek," "should," or "will," or the negative thereof or other variations thereon or comparable terminology. All forward-looking statements, including, without limitation, management's examination of historical operating trends and data are based upon our current expectations and various assumptions. We have based these forward-looking statements on our current expectations, assumptions, estimates and projections. While we believe these expectations, assumptions, estimates and projections are reasonable, such forward-looking statements are only predictions and involve known and unknown risks and uncertainties, many of which are beyond our control. These and other important factors may cause our actual results, performance or achievements to differ materially from any future results, performance or achievements expressed or implied by these forward-looking statements.

Some of the factors that could cause actual results to differ materially from those expressed or implied by the forward-looking statements include, among others:

- risks associated with our substantial indebtedness and debt service, including our need to comply with various negative and other covenants contained in our debt agreements;
- risks associated with our ability to access existing liquidity and/or access the debt or equity markets;
- increases in prices and availability of resin and other raw materials, our ability to pass these increased costs on to our customers and our ability to raise our prices generally with respect to our products;
- our ability to retain management;
- risks of increasing competition in our existing and future markets, including competition from new products introduced by competitors;
- our ability to meet future capital requirements;
- general economic or business conditions, both in the U.S. and worldwide;
- risks related to our acquisition or divestiture strategy;
- our ability to protect our intellectual property rights;
- changes in governmental laws and regulations, including environmental laws and regulations;
- changes in foreign currency exchange rates; and
- other risks and uncertainties, including those described in the "Risk Factors" section of our Annual Report on Form 10-K for the fiscal year ended December 31, 2010 filed with the SEC.

Given these risks and uncertainties, you are cautioned not to place undue reliance on such forward-looking statements. The forward-looking statements included in this report are made only as of the date hereof. We do not undertake and specifically decline any obligation to update any such statements or

to publicly announce the results of any revisions to any of such statements to reflect future events or developments.

## **OVERVIEW**

We are an international manufacturer, marketer and supplier of protective packaging products and specialty packaging solutions. We currently operate 46 facilities in 18 countries, with approximately 4,000 employees world-wide. We sell our products to a wide array of customers, including retailers, distributors, packer processors, hospitals, fabricators and directly to the end-users. Approximately 63% of our 2010 net sales were generated outside of the U.S., so we are sensitive to fluctuations in foreign currency exchange rates, primarily between the euro and pound sterling with the U.S. dollar.

Our net sales for the three months ended March 31, 2011 increased 8.1% over the comparable period of 2010. The increase was driven primarily by the impact of selling price increases, increased volumes from the Company's growth initiatives, and incremental sales associated with the acquisition of IntelliPack, partially offset by unfavorable foreign currency translation. Excluding the impact of unfavorable foreign currency translation and the net sales of the partial quarter of IntelliPack, net sales for the three months ended March 31, 2011 increased 7.4% compared to the same period in 2010.

Our gross margin (defined as net sales less cost of sales, excluding depreciation and amortization) as a percent of net sales decreased to 21.4% for the first quarter of 2011, compared to 22.6% for the same period of 2010. The decline in our 2011 gross margin percentage was driven primarily by increased key raw material costs partially offset by the impact of selling price increases. The majority of the products we sell are plastic-resin based, and therefore our operations are highly sensitive to fluctuations in the costs of plastic resins. In the first quarter of 2011 as compared to the same period of 2010, average resin costs increased approximately 12% in North America and 30% in Europe, as measured by the Chemical Market Associates, Inc. ("CMAI") index and ICIS index, their respective market indices.

On March 23, 2011, the Company successfully refinanced its existing \$50 million revolving credit facility with a new \$75 million ABL credit facility. This refinancing addressed the October 2011 maturity of our old revolving credit facility while providing additional liquidity.

## RESULTS OF OPERATIONS

### Net Sales

Our net sales for the three months ended March 31, 2011 compared to the same period ended March 31, 2010 are summarized by segment as follows:

	Three Months Ended March 31,		\$ Change	% Change	Change Attributable to the Following Factors							
	2011	2010			Price / Mix	Volume	Acquisition	Currency Translation				
	(dollars in thousands)											
<b>Segment:</b>												
Protective Packaging	\$ 146,018	\$ 134,860	\$11,158	8.3%	\$ 7,010	5.2%	\$2,776	2.1%	\$2,339	1.7%	\$(967)	(0.7)%
Specialty Packaging	80,980	75,176	5,804	7.7%	4,213	5.6%	1,577	2.1%	—	—%	14	0.0%
Total	<u>\$ 226,998</u>	<u>\$ 210,036</u>	<u>\$16,962</u>	8.1%	<u>\$11,223</u>	5.3%	<u>\$4,353</u>	2.1%	<u>\$2,339</u>	1.1%	<u>\$(953)</u>	<u>(0.4)%</u>

### Segment Net Sales

Volume in the Company's protective packaging segment increased by 2.1% for the three month period ended March 31, 2011 compared to the same period in 2010. The volume increase for the period was driven primarily by the Company's growth initiatives in products such as Honeycomb paper products, inflatable systems, and sustainable products.

Price/mix for the Company's protective packaging segment increased net sales by 5.2% for the three month period ended March 31, 2011 compared to the same period in 2010. Price/mix was favorable year-over-year due to selling price increases implemented in both our North American and European businesses in response to increased key raw material costs.

Volume in the Company's specialty packaging segment increased by 2.1% for the three month period ended March 31, 2011 compared to the same period of 2010, primarily due to the impact of growth initiatives in our fresh food packaging markets.

Price/mix for the Company's specialty packaging segment increased net sales by 5.6% for the year ended March 31, 2011 compared to the same period in 2010. Price/mix was favorable year-over-year due primarily to selling price increases implemented in our flexible packaging business in response to increased key raw material costs.

### Gross Margin

Gross margin (defined as net sales less cost of sales, excluding depreciation and amortization), as a percent of net sales, was 21.4% for the three months ended March 31, 2011 compared to 22.6% for the same period of 2010. This decrease of 120 basis points was driven by increased key raw material costs partially offset by the impact of selling price increases and increased volumes. The increase in key raw material costs resulted in a negative 187 basis point impact on gross margin as a percent of net sales.

Average resin costs in North America for the three month period ended March 31, 2011 were 12% higher than average resin costs for the same period in 2010 while average resin costs in Europe were 30% higher than average resin prices for the same period of 2010, based on their respective market indices.

### ***Selling, General and Administrative Expenses***

Selling, general and administrative expenses decreased by \$3.8 million for the three months ended March 31, 2011 compared to the same period of 2010. This decrease was primarily driven by decreased legal expenses and 2010 acquisition related fees not incurred in 2011, partially offset by 2011 severance expense and incremental IntelliPack expenses for the full quarter of 2011 compared to a partial quarter in 2010. The 2010 legal expenses were the result of a patent dispute related to the Company's protective packaging segment. In March 2010, there was an initial ruling which was favorable to the Company. As of March 31, 2011 there is a pending appeal regarding this legal matter which the Company also believes will have a favorable outcome to the Company. Excluding the impact of the legal expenses and acquisition related costs, selling, general and administrative expenses for the three months ended March 31, 2011 increased by approximately \$1.5 million due primarily to severance expense, a full quarter of IntelliPack expenses in 2011 compared to a partial quarter in 2010, and increased sales and marketing expenses incurred to help drive the Company's growth initiatives.

### ***Other Operating Expense, net***

For the three months ended March 31, 2011, other operating expense, net totaled \$0.3 million, compared to \$0.6 million in the same period of 2010. In the 2011 period we recorded restructuring charges of \$0.5 million, primarily related to consulting expenses. In the 2010 period we recorded restructuring charges of \$0.6 million primarily related to consulting expenses. See Note 9 to the unaudited consolidated financial statements for details regarding our restructuring activity.

### ***Depreciation and Amortization Expense***

Depreciation and amortization expense increased by \$1.2 million for the three months ended March 31, 2011, compared to the respective period of 2010, primarily due to the IntelliPack acquisition.

### ***Segment Income***

We measure our segments' operating performance on the basis of segment EBITDA, defined as net income (loss) before interest, taxes, depreciation, amortization, and restructuring expense and adjusted for other non-cash charges and benefits. See Note 11 to the unaudited consolidated financial statements for a reconciliation of total segment EBITDA to consolidated net loss before income taxes. Segment EBITDA for the relevant periods is as follows:

	<u>Three Months Ended March 31,</u>		<u>\$ Change</u>	<u>% Change</u>
	<u>2011</u>	<u>2010</u>		
	<u>(dollars in thousands)</u>			
<b>Segment:</b>				
Protective Packaging	\$ 12,175	\$ 10,781	\$ 1,394	12.9%
Specialty Packaging	9,094	9,544	(450)	(4.7)%
Total segment EBITDA	<u>\$ 21,269</u>	<u>\$ 20,325</u>	<u>\$ 944</u>	4.6%

Segment EBITDA for the Protective Packaging segment increased \$1.4 million for the three months ended March 31, 2011 compared to the same period of 2010. This increase was primarily due to the

impact from selling price increases, increased volumes, and the impact of the IntelliPack acquisition partially offset by increased key raw material costs.

Segment EBITDA for specialty packaging decreased by \$0.5 million for the first quarter of 2011. This decrease was due to significantly higher key raw material costs which were only partially offset by favorable pricing.

#### ***Interest Expense***

Interest expense for the three months ended March 31, 2011 increased \$1.1 million compared to the same period of 2010. The increase was primarily driven by the termination of the interest rate swap contract in March 2011, which resulted in \$0.8 million of additional interest expense. In addition, unfavorable foreign currency increased interest expense on the Company's euro denominated debt.

#### ***Foreign Exchange Loss (Gain), net***

A portion of our third-party debt is denominated in euro and revalued to U.S. dollars at month-end. We also maintain an intercompany debt structure, whereby Pregis Corporation has provided euro-denominated loans to certain of its foreign subsidiaries and these and other foreign subsidiaries have provided euro-denominated loans to certain U.K. based subsidiaries. At each month-end we recognize unrealized gains and losses on the revaluation of these instruments, resulting from the fluctuations between the U.S. dollar and euro exchange rate, as well as the pound sterling and euro exchange rate.

In the three months ended March 31, 2011, we recognized a net foreign exchange gain of \$1.1 million. The gain in the quarter reflects the relative weakening of the U.S. dollar at the end of March 2011 (relative to December 31, 2010 exchange rates) when we revalued our euro-denominated third-party debt and inter-company loans. In the three month period ended March 31, 2010, we recognized a net foreign exchange loss of \$1.3 million.

#### ***Income Tax Expense***

Our effective income tax rate was approximately 14.89% for the three months ended March 31, 2011, which compares to approximately 15.23% for the three months ended March 31, 2010. For the three months ended March 31, 2011 and 2010, the Company's effective rate differs from the U.S. federal statutory rate of 35% primarily due to the establishment of additional valuation allowances against losses in certain jurisdictions that are not expected to result in future tax benefits.

#### ***Net Loss***

For the three months ended March 31, 2011, we had a net loss of \$7.7 million, compared to a net loss of \$12.2 million in the comparable period of 2010. As discussed herein, the 2011 net loss is mainly the result of increased raw material costs partially offset by increases in selling prices and increased sales volumes.

## LIQUIDITY AND CAPITAL RESOURCES

The following table shows our sources and uses of funds for the three months ended March 31, 2011 compared to the three months ended March 31, 2010:

	<u>Three Months Ended March 31,</u>	
	<u>2011</u>	<u>2010</u>
	<u>(dollars in thousands)</u>	
Cash provided (used) in operating activities	\$ (5,873)	\$ 1,959
Cash used in investing activities	(8,465)	(41,627)
Cash provided (used) in financing activities	(3,542)	484
Effect of foreign exchange rate changes	1,101	(1,787)
Decrease in cash and cash equivalents	<u>\$(16,779)</u>	<u>\$(40,971)</u>

**Operating Activities.** Cash used in operating activities increased by \$7.8 million during the three months ended March 31, 2011 compared to the same period of 2010. This increase was driven primarily by increased working capital investment due to the increased year-over-year sales volumes, as well as increased key raw material costs.

Cash from operating activities is sensitive to raw material costs and the Company's ability to recover increases in these costs from its customers. Although price increases have typically lagged the underlying change in raw material costs, the Company has historically been able to recover significant increases in underlying raw material costs from its customers over a twelve to twenty-four month period. Future cash from operations is dependent upon the Company's continued ability to recover increases in underlying raw material increases from its customers.

The Company has not experienced any significant changes in year-over-year days sales outstanding, days inventory on-hand or days payable outstanding. The Company has not identified any trends in key working capital investments that would have a material impact on its liquidity or ability to satisfy its debt obligations or fund capital expenditures. Significant increases in resin pricing could negatively affect our cash generated from operating activities in future periods.

**Investing Activities.** Cash used in investing activities totaled \$8.5 million for the three months ended March 31, 2011, a decrease of \$33.2 million compared to the same period of 2010. This decrease was primarily the result of the 2010 acquisition of IntelliPack. In February 2010, Pregis acquired all of the stock of IntelliPack for an initial purchase price of \$31.5 million and certain escrowed amounts totaling \$3.5 million, which was funded with cash-on-hand. Capital expenditures totaled \$8.4 million in the 2011 period compared to \$6.8 million in the 2010 period, driven by investments for capacity expansion in our specialty segment.

**Financing Activities.** Cash used in financing activities for the three months ended March 31, 2011 increased \$4.0 million compared to the same period of 2010. This increase was a result of the repayment of the senior secured credit facility of \$43.0 million and deferred financing fees incurred in connection with the ABL credit facility of \$1.1 million partially offset by proceeds from a draw on the ABL credit facility of \$40.1 million.

Our liquidity requirements are significant, primarily due to debt service requirements and capital investment in our businesses. We expect our 2011 capital expenditures to total approximately \$30 to \$35 million and our 2011 debt service costs to total approximately \$40 million. At March 31, 2011, we had cash and cash equivalents of \$31.1 million. Our available cash and cash equivalents are held in bank

deposits and money market funds. We actively monitor the third-party depository institutions that hold our cash and cash equivalents to ensure safety of principal while achieving a satisfactory yield on those funds. To date, we have experienced no material loss or lack of access to our invested cash or cash equivalents; however, we can provide no assurances that access to our invested cash and cash equivalents will not be impacted by adverse conditions in the financial markets.

Our primary source of liquidity will continue to be cash flows from operations, existing cash balances, and amounts available to the Company under the ABL credit facility and foreign lines of credit.

**ABL Credit Facility.** On March 23, 2011, Pregis Holding II and Pregis and certain of their subsidiaries entered into a \$75 million Credit Agreement with Wells Fargo Capital Finance, LLC, as agent, Wells Fargo Bank, National Association, as lender and other lenders from time to time parties thereto (“ABL credit facility”). The ABL credit facility provides for the borrowings in dollars, euros and pounds sterling and consists of (1) a UK facility, under which certain UK subsidiaries of Pregis (the “UK Borrowers”) may from time to time borrow up to a maximum amount of the lesser of the UK borrowing base and \$30 million and (2) a US facility, under which certain US subsidiaries of Pregis (the “US Borrowers” and, together with the UK Borrowers, the “Borrowers”) may from time to time borrow up to a maximum amount of the lesser of the US borrowing base and \$75 million less amounts outstanding under the UK facility. The borrowing base is calculated on the basis of certain permitted over advance amounts, plus a percentage of certain eligible accounts receivable and eligible inventory, subject to reserves established by the agent from time to time. The ABL credit facility provides for the issuances of letters of credit and a swingline subfacility. The ABL credit facility also provides for future uncommitted increases of its maximum amount, not to exceed \$40 million.

The ABL credit facility matures on the earlier of March 22, 2016 and the date that is 90 days prior to the maturity of the existing high yield notes of Pregis Corporation (as such notes may be refinanced prior to such maturity date). Advances under the ABL credit facility bear interest, at the Borrowers’ option, equal to adjusted LIBOR plus an applicable margin for LIBOR loans or a base rate plus an applicable margin for base rate loans. The applicable margin for LIBOR loans ranges from 2.5% to 3%, depending on the average quarterly excess availability of the Borrowers. The applicable margin for the base rate loans is 100 basis points lower than the applicable margin for the LIBOR loans.

All obligations under the ABL credit facility are guaranteed by Pregis Holding II and certain of its direct and indirect subsidiaries (other than certain non wholly-owned and immaterial subsidiaries and certain foreign subsidiaries), with foreign guarantors guaranteeing only the obligations of the UK Borrowers. All obligations under the ABL credit facility and the guarantees of those obligations are secured, subject to certain exceptions, by a first-priority security interest in substantially all assets of the Pregis Holding II, the Borrowers and the guarantors, as well as the pledge of 100% of the capital stock of the Borrowers, the guarantors and their direct subsidiaries, with the obligations of the US Borrowers being secured only by (1) a first-priority security interest in substantially all assets of the Pregis Holding II, the US Borrowers and the domestic guarantors, (2) a pledge of 100% of the capital stock of the US Borrowers, the domestic guarantors and their direct domestic subsidiaries and (3) a pledge of 65% of the voting capital stock and 100% of the non-voting capital stock of the first-tier foreign subsidiaries of the US Borrowers and domestic guarantors. The security interest in the domestic collateral ranks prior to the security interest securing the Company’s existing second priority floating rate notes due 2013. The lenders under the ABL credit facility have agreed to share their domestic collateral with future secured notes, if any, that refinance the existing notes, with the ABL credit facility retaining a first priority security interest in all accounts receivable, inventory and certain related assets of the Pregis Holding II, the US Borrowers and the domestic guarantors and subordinating its security interest in all other domestic assets and the capital stock of the US Borrowers, domestic guarantors and their direct subsidiaries to the liens securing such new secured notes, if any.

The ABL credit facility contains customary representations, warranties, covenants and events of default, and requires monthly compliance with a “springing” fixed charge coverage ratio of 1.1 to 1.0 if the excess availability of Pregis and its subsidiaries falls below a certain level. The ABL credit facility is also subject to mandatory prepayments out of certain asset sale, insurance and condemnation proceeds, if the excess availability of Pregis and its subsidiaries falls below a certain level.

As of March 31, 2011, borrowings under the ABL credit facility totaled \$40,084, outstanding letters of credit were \$6,750, and remaining availability was \$28,166. The Company utilized proceeds from the ABL to pay off and terminate its pre-existing \$50 million revolving credit facility.

***Senior Secured Floating Rate Notes and Senior Subordinated Notes.*** On October 13, 2005, Pregis issued €100.0 million aggregate principal amount of second priority senior secured floating rate notes due 2013 (the “senior secured notes”) and \$150 million aggregate principal amount of 12.375% senior subordinated notes due 2013 (the “senior subordinated notes”).

The senior secured notes mature on April 15, 2013. Interest accrues at a floating rate equal to EURIBOR plus 5.00% per year and is payable quarterly on January 15, April 15, July 15 and October 15 of each year. The senior secured notes are guaranteed on a senior secured basis by Pregis Holding II, Pregis’s immediate parent, and each of Pregis’s current and future domestic subsidiaries. At its option, Pregis may redeem some or all of the senior secured notes at 100% of their principal amount. Upon the occurrence of a change of control, Pregis will be required to make an offer to repurchase each holder’s notes at a repurchase price equal to 101% of their principal amount, plus accrued and unpaid interest to the date of repurchase.

The senior subordinated notes mature on October 15, 2013. Interest accrues at a rate of 12.375% and is payable semi-annually on April 15 and October 15 of each year. The notes are senior subordinated obligations and rank junior in right of payment to all of Pregis’s senior indebtedness. The senior subordinated notes are guaranteed on a senior subordinated basis by Pregis Holding II and each of Pregis’s current and future domestic subsidiaries. Pregis may redeem some or all of the notes at redemption prices equal to 103.094% of their principal amount (in the 12 months beginning October 15, 2010) and 100% of their principal amount (beginning October 15, 2011).

On October 5, 2009 Pregis issued €125.0 million aggregate principal amount of additional second priority senior secured floating rate notes due 2013 (the “2009 senior secured notes”). The 2009 senior secured notes are treated as a single class under the indenture with the €100.0 million principal amount of 2005 second priority senior secured floating rate notes for purpose of voting and redemption. However, the 2009 senior secured notes do not have the same Common Code or ISIN numbers as the 2005 senior secured notes, are not fungible with the 2005 senior secured notes and will not trade together as a single class with the 2005 senior secured notes. The 2009 senior secured notes are treated as issued with more than de minimis original issue discount for United States federal income tax purposes, whereas the 2005 senior secured notes were not issued with original issue discount for such purposes. Together the 2005 senior secured notes and the 2009 senior secured notes are referred to herein as the senior secured notes.

The indentures governing the senior secured notes and the senior subordinated notes contain covenants that limit or prohibit Pregis’s ability and the ability of its restricted subsidiaries, subject to certain exceptions, to incur additional indebtedness, pay dividends or make other equity distributions, make investments, create liens, incur obligations that restrict the ability of Pregis’s restricted subsidiaries to make dividends or other payments to Pregis, sell assets, engage in transactions with affiliates, create unrestricted subsidiaries, and merge or consolidate with other companies or sell substantially all of Pregis’s assets. The indentures also contain reporting covenants regarding delivery of annual and quarterly financial information. The indenture governing the senior secured notes limits Pregis’s ability to incur first priority secured debt to an amount which results in its secured debt leverage ratio being greater than 3:1, plus \$50 million, and prohibits it from incurring additional second priority secured debt other

than by issuing additional senior secured notes. The indenture governing the senior secured notes also limits Pregis's ability to enter into sale and leaseback transactions. The indenture governing the senior subordinated notes prohibits Pregis from incurring debt that is senior to such notes and subordinate to any other debt.

The senior secured notes and senior subordinated notes are not listed on any national securities exchange in the United States. The senior secured notes are listed on the Irish Stock Exchange. However, there can be no assurance that the senior secured notes will remain listed.

**Collateral for the Senior Secured Floating Rate Notes.** The senior secured floating rate notes are secured by a second priority lien, subject to permitted liens, on all of the following assets owned by Pregis or the guarantors, to the extent such assets secure Pregis's senior secured credit facilities on a first priority basis (subject to exceptions):

- (1) substantially all of Pregis's and each guarantor's existing and future property and assets, including, without limitation, real estate, receivables, contracts, inventory, cash and cash accounts, equipment, documents, instruments, intellectual property, chattel paper, investment property, supporting obligations and general intangibles, with minor exceptions; and
- (2) all of the capital stock or other securities of Pregis's and each guarantor's existing or future direct or indirect domestic subsidiaries and 66% of the capital stock or other securities of Pregis's and each guarantor's existing or future direct foreign subsidiaries, but only to the extent that the inclusion of such capital stock or other securities will mean that the par value, book value as carried by us, or market value (whichever is greatest) of such capital stock or other securities of any subsidiary is not equal to or greater than 20% of the aggregate principal amount of the senior secured floating rate notes outstanding.

As of December 31, 2010, the capital stock of the following subsidiaries of Pregis constituted collateral for the senior secured floating rate notes:

Name of Subsidiary	As of December 31, 2010		
	Amount of Collateral (Maximum of Book Value and Market Value, Subject to 20% Cap)	Book Value of Capital Stock	Market Value of Capital Stock
Pregis Innovative Packaging Inc.	\$60,165,000	\$50,300,000	\$112,300,000
Hexacomb Corporation	\$43,400,000	\$43,300,000	\$ 37,200,000
IntelliPack	\$38,300,000	\$38,300,000	\$ 9,100,000
Pregis (Luxembourg) Holding S.à.r.l. (66%)	\$17,300,000	\$17,300,000	\$ —
Pregis Management Corporation	\$ 100	\$ 100	\$ 100

As described above, under the collateral agreement, the capital stock pledged to the senior secured noteholders constitutes collateral only to the extent that the par value or market value or book value (whichever is greatest) of the capital stock does not exceed 20% of the aggregate principal amount of the senior secured notes. This threshold is €45,000,000, or, at the December 31, 2010 exchange rate of U.S. dollars to euro of 1.3370:1.00, approximately \$60.2 million. As of December 31, 2010, the book value and the market value of the shares of capital stock of Pregis Innovative Packaging Inc. were

approximately \$50.3 million and \$112.3 million, respectively; the book value and the market value of the shares of capital stock of Hexacomb Corporation were approximately \$43.3 million and \$37.2 million respectively; the book value of and the market value of the shares of capital stock of IntelliPack were approximately \$38.3 million and \$9.1 million respectively; and the book value and the market value of 66% of the shares of capital stock of Pregis (Luxembourg) Holding S.à.r.l. were approximately \$17.3 million and \$— million, respectively. Therefore, in accordance with the collateral agreement, the collateral pool for the senior secured floating rate notes includes approximately \$60.2 million with respect to the shares of capital stock of Pregis Innovative Packaging Inc. Since the book value and market value of the shares of capital stock of our other domestic subsidiaries and Pregis (Luxembourg) Holdings S.à.r.l are each less than the \$60.2 million threshold, they are not effected by the 20% clause of the collateral agreement.

For purposes of calculating book value for the year ended December 31, 2010 in the table above, certain historical equity relating to corporate expenses incurred by Pregis Management Corporation were allocated to each of the three entities, Pregis Innovative Packaging Inc., Hexacomb Corporation, and Pregis (Luxembourg) Holding S.à.r.l, in order to better reflect their current book values for presentation herein on a fully-allocated basis.

The market value of the capital stock of the guarantors and subsidiaries constituting collateral for the senior secured notes has been estimated by us on an annual basis, using a market approach. At the time of the Acquisition, the purchase price paid for these entities was determined based on a multiple of EBITDA, as was contractually agreed in the stock purchase agreement. Since that time, we have followed a similar methodology, using a multiple of EBITDA, based on that of recent transactions of comparable companies, to determine the enterprise value of these entities. To arrive at an estimate of the market value of the entities' capital stock, we have subtracted from the enterprise value the existing debt, net of cash on hand, and have also made adjustments for the businesses' relative portion of corporate expenses. We have determined that this methodology is a reasonable and appropriate means for determining the market value of the capital stock pledged as collateral. We intend to complete these estimates of value of the capital stock of these subsidiaries for so long necessary to determine our compliance with the collateral arrangement governing the notes.

The value of the collateral for the senior secured notes at any time will depend on market and other economic conditions, including the availability of suitable buyers for the collateral. As of December 31, 2010, the value of the collateral for the senior secured floating rate notes totaled approximately \$617.7 million, estimated as the sum of (1) the book value of the total assets of Pregis and each guarantor, excluding intercompany activity (which amount totaled \$459.2 million), and (2) the collateral value of the capital stock, as outlined above (which amount totaled \$158.5 million). Any proceeds received upon the sale of collateral would be paid first to the lenders under our ABL credit facility, who have a first lien security interest in the collateral, before any payment could be made to holders of the senior secured notes. There is no assurance that any collateral value would remain for the holders of the senior secured notes after payment in full to the lenders under our ABL credit facility.

***Covenant Ratios Contained in the Senior Secured Notes and Senior Subordinated Notes.*** The indentures governing the senior secured notes and senior subordinated notes contain two material covenants which utilize financial ratios. Non-compliance with these covenants could result in an event of default under the indentures and, under certain circumstances, a requirement to immediately repay all amounts outstanding under the notes and could trigger a cross-default under Pregis's ABL credit facility or other indebtedness we may incur in the future. First, Pregis is permitted to incur indebtedness under the indentures if the ratio of Consolidated Cash Flow to Fixed Charges on a pro forma basis (referred to in the indentures as the "Fixed Charge Coverage Ratio") is greater than 2:1 or, if the ratio is less, only if the indebtedness falls into specified debt baskets, including, for example, a credit agreement debt basket, an existing debt basket, a capital lease and purchase money debt basket, an intercompany debt basket, a permitted guarantee debt basket, a hedging debt basket, a receivables transaction debt basket and a

general debt basket. In addition, under the senior secured floating rate notes indenture, Pregis is permitted to incur first priority secured debt only if the ratio of Secured Indebtedness to Consolidated Cash Flow on a pro forma basis (referred to in the senior secured floating rate notes indenture as the “Secured Indebtedness Leverage Ratio”) is equal to or less than 3:1, plus \$50 million. Second, the restricted payment covenant provides that Pregis may declare certain dividends, or repurchase equity securities, in certain circumstances only if Pregis’s Fixed Charge Coverage Ratio is greater than 2:1.

As used in the calculation of the Fixed Charge Coverage Ratio and the Secured Indebtedness Leverage Ratio, Consolidated Cash Flow, commonly referred to as Adjusted EBITDA, is calculated by adding Consolidated Net Income, income taxes, interest expense, depreciation and amortization and other non-cash expenses, amounts paid pursuant to the management agreement with AEA Investors LP, and the amount of any restructuring charge or reserve (including, without limitation, retention, severance, excess pension costs, contract termination costs and cost to consolidate facilities and relocate employees). In calculating the ratios, Consolidated Cash Flow is further adjusted by giving pro forma effect to acquisitions and dispositions that occurred in the prior four quarters, including certain cost savings and synergies expected to be obtained in the succeeding twelve months. In addition, the term Net Income is adjusted to exclude any gain or loss from the disposition of securities, and the term Consolidated Net Income is adjusted to exclude, among other things, the non-cash impact attributable to the application of the purchase method of accounting in accordance with GAAP, the cumulative effect of a change in accounting principles, and other extraordinary, unusual or nonrecurring gains or losses. While the determination of appropriate adjustments is subject to interpretation and requires judgment, we believe the adjustments listed below are in accordance with the covenants discussed above.

The following table sets forth the Fixed Charge Coverage Ratio, Consolidated Cash Flow (“Adjusted EBITDA”), Secured Indebtedness Leverage Ratio, Fixed Charges and Secured Indebtedness as of and for the twelve months ended March 31, 2011 and 2010:

(unaudited) (dollars in thousands)	Covenant Measure	Ratios	
		Calculated at March 31,	
		2011	2010
Fixed Charge Coverage Ratio (after giving pro forma effect to acquisitions and/or dispositions occurring in the reporting period)	Minimum of 2.0x	1.8x	2.1x
Secured Indebtedness Leverage Ratio	Maximum of 3.0x	0.6x	0.5x
Consolidated Cash Flow (“Adjusted EBITDA”)	—	\$76,638	\$87,980
Fixed Charges (after giving pro forma effect to acquisitions and/or dispositions occurring in the reporting period)	—	\$42,797	\$41,429
Secured Indebtedness	—	\$44,513	\$43,061

The Fixed Charge Coverage Ratio is primarily affected by increases or decreases in the Company’s trailing twelve month Consolidated Cash Flow (Adjusted EBITDA) and increases or decreases in the Company’s interest expense (interest expense net of interest income, excluding amortization of deferred financing fees and discount). Interest expense as used in this ratio is primarily affected by changes in interest rates (LIBOR and EURIBOR) and currency translation related to converting euro based interest expense into US dollars. The favorable impact resulting from lower interest rates, for the comparable twelve month periods ending March 31, 2011 and 2010, has been more than offset by the decrease in the Company’s trailing twelve month Consolidated Cash Flow over the same period, resulting in a reduction in the actual ratio. As of March 31, 2011, the Company’s Fixed Charge Coverage Ratio was less than 2:0. As a result the Company’s ability to borrow money was limited to its available debt baskets, including among others a \$220 million credit facility basket, a \$25

million general basket (which has been used in part in order to incur debt under Pregis's ABL credit facility), and a \$15 million capital lease basket.

Adjusted EBITDA is calculated under the indentures governing our senior secured floating rate notes and senior subordinated notes for the twelve months ended March 31, 2011 and 2010 as follows:

(unaudited) (dollars in thousands)	Twelve Months Ended March 31,	
	2011	2010
Net loss of Pregis Holding II Corporation	\$ (32,603)	\$ (19,810)
Interest expense, net of interest income	49,275	44,805
Income tax (benefit) expense	(8,087)	(1,523)
Depreciation and amortization	<u>47,629</u>	<u>44,506</u>
EBITDA	56,214	67,978
Other non-cash charges (income): (1)		
Unrealized foreign currency transaction losses (gains), net	(1,167)	(8,369)
Non-cash stock based compensation expense	2,663	1,585
Non-cash asset impairment charge	—	(59)
Other non-cash expenses, primarily fixed asset disposals and write-offs	1,837	—
Net unusual or nonrecurring gains or losses: (2)		
Restructuring, severance and related expenses	9,456	10,604
Other unusual or nonrecurring gains or losses	5,616	10,735
Other adjustments: (3)		
Amounts paid pursuant to management agreement with Sponsor	2,019	2,514
Pro forma adjusted EBITDA of acquired business (4)	—	2,992
Adjusted EBITDA ("Consolidated Cash Flow")	<u>\$ 76,638</u>	<u>\$ 87,980</u>

- (1) Other non-cash charges (income) include (a) net unrealized foreign currency transaction losses and gains, arising principally from the revaluation of our euro-denominated third-party debt and intercompany notes receivable, (b) non-cash compensation expense arising from the grant of Pregis Holding I options, and (c) other non-cash charges that will not result in future cash settlement, such as losses on fixed asset disposals.
- (2) As provided by our indentures, we adjusted for gains or losses deemed to be unusual or nonrecurring, including (a) restructuring, severance and related expenses due to our various cost reduction restructuring initiatives, (b) adjustments for costs and expenses related to acquisition, disposition or equity offering activities and (c) other unusual and nonrecurring charges.
- (3) Our indentures also require us to make adjustments for fees, and reasonable out-of-pocket expenses, paid under the management agreement with AEA Investors LP.
- (4) Our indentures also permit adjustments to net income on a pro forma basis which allow for the inclusion of earnings for acquired businesses as if the acquisition had occurred on the first day of the four-quarter measurement period. In the three months ended March 31, 2010, we have adjusted for approximately \$3.0 million relating to pre-acquisition earnings relating to the acquisition of IntelliPack. There can be no assurance that we will be able to achieve these comparable earning in the future.

**Local lines of credit.** From time to time, certain of our foreign businesses utilize various lines of credit in their operations. These lines of credit are generally used as overdraft facilities or for the issuance of trade letters of credit and are in effect until cancelled by one or both parties. As of March 31, 2011, we

had availability of \$1.5 million on these lines and outstanding trade letters of credit and guarantees totaling \$3.6 million.

**Long-term Liquidity.** We believe that cash flow generated from operations, existing cash balances, and our borrowing capacity will be adequate to meet our obligations and business requirements for the next twelve months. There can be no assurance, however, that our business will generate sufficient cash flow from operations, that anticipated net sales growth and operating improvements will be realized or that future borrowings will be available under Pregis's senior secured credit facilities in an amount sufficient to enable us to service our indebtedness or to fund our other liquidity needs. Our ability to meet our debt service obligations and other capital requirements, including capital expenditures, and to continue to comply with the covenants contained in our debt instruments, will depend upon our future performance which, in turn, will be subject to general economic, financial, business, competitive, legislative, regulatory and other conditions, many of which are beyond our control. Some other risks that could materially adversely affect our ability to meet our debt service obligations and comply with our debt covenants include, but are not limited to, risks related to increases in the cost of resin, our ability to protect our intellectual property, rising interest rates, a decline in the overall U.S. and European economies, weakening in our end markets, the loss of key personnel, our ability to continue to invest in equipment, and a decline in relations with our key distributors and dealers. In addition, any of the other items discussed in the "Risk Factors," included in our Annual Report on Form 10-K for the year ended December 31, 2010 may also significantly impact our liquidity and covenant compliance.

## **CRITICAL ACCOUNTING POLICIES AND ESTIMATES**

In accordance with ASC 350, the Company assesses the recoverability of goodwill and other indefinite lived intangibles assets annually as of October 1, or whenever events or changes in circumstances indicate that the carrying value of such assets may not be recoverable.

The goodwill impairment test is performed at the reporting unit level. A reporting unit is an operating segment or one level below an operating segment (referred to as a "component"). A component is considered a reporting unit for purposes of goodwill testing if the component constitutes a business for which discrete financial information is available and segment management regularly reviews the operating results of that component. As such, we have tested for goodwill impairment at the component level within our Specialty Packaging reporting segment, represented by each of the businesses included within this segment. We also tested goodwill for impairment at each of the operating segments which have been aggregated to comprise our Protective Packaging reporting segment.

We use a two-step process to test goodwill for impairment. First, the reporting unit's fair value is compared to its carrying value. Fair value is estimated using primarily a combination of the income approach, based on the present value of expected future cash flows and the market approach. If a reporting unit's carrying amount exceeds its fair value, an indication exists that the reporting unit's goodwill may be impaired, and the second step of the impairment test would be performed. The second step of the goodwill impairment test is used to measure the amount of the impairment loss, if any. In the second step, the implied fair value of the reporting unit's goodwill is determined by allocating the reporting unit's fair value to all of its assets and liabilities other than goodwill in a manner similar to a purchase price allocation. The implied fair value of the goodwill that results from the application of this second step is then compared to the carrying amount of the goodwill and an impairment charge would be recorded for the difference if the carrying value exceeds the implied fair value of the goodwill.

At interim periods, the Company assesses if potential indicators of impairment exist. Among the factors the Company considers as potential indicators of interim impairment are significant adverse changes in legal factors or business climate, an adverse action or assessment by a regulator, unanticipated competition, loss of key personnel, or a more-likely-than-not expectation that a reporting

unit or a significant portion of a reporting unit will be sold or otherwise disposed of, recent operating losses at the reporting unit level, downward revisions to forecasts, restructuring actions or plans, and industry trends. The Company did not identify any interim indicators of impairment as of March 31, 2011.

Although the Company determined that there were no indicators of impairment as of March 31, 2011, it is possible that the future occurrence of potential indicators of impairment could require an interim assessment for some or all of the Company's reporting units prior to its next required annual assessment. In such circumstances, the Company may be required to recognize non-cash impairment charges which could be material to the Company's consolidated financial position and results of operations. Such non-cash impairment charges would not have a material adverse impact on the Company's ability to comply with its debt covenants, as such charges are specifically excluded from its covenant calculations.

Our financial statements are prepared in accordance with generally accepted accounting principles in the United States, which require management to make estimates, judgments and assumptions that affect the amounts reported in the financial statements and accompanying notes. While our estimates and assumptions are based on our knowledge of current events and actions we may undertake in the future, actual results may ultimately differ from these estimates and assumptions. We have discussed those estimates that we believe are critical and require the use of complex judgment in their application in our 2010 Annual Report on Form 10-K. Since the date of our 2010 Form 10-K, there have been no material changes to our critical accounting policies or the methodologies or assumptions we apply under them.

### **Item 3. Quantitative and Qualitative Disclosures About Market Risk**

Our exposure to market risk has not materially changed since December 31, 2010. For a discussion of our exposure to market risk, see our 2010 Annual Report on Form 10-K.

### **Item 4. Controls and Procedures**

The Company carried out an evaluation, under the supervision and with the participation of the Company's management, including the Chief Executive Officer (its principal executive officer) and the Chief Financial Officer (its principal financial officer), of the effectiveness of the design and operation of the Company's disclosure controls and procedures as of March 31, 2011. Based upon that evaluation, our management, including our Chief Executive Officer and our Chief Financial Officer, concluded that as of March 31, 2011 the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, as amended) are effective. In addition, there has been no change in the Company's internal control over financial reporting during the most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

## **PART II — OTHER INFORMATION**

### **Item 1. Legal Proceedings**

We are party to various lawsuits, legal proceedings and administrative actions arising out of the normal course of our business. While it is not possible to predict the outcome of any of these lawsuits, proceedings and actions, management, based on its assessment of the facts and circumstances now known, does not believe that any of these lawsuits, proceedings and actions, individually or in the aggregate, will have a material adverse effect on our financial position or that it is reasonably possible that a loss exceeding amount already recognized may be material. However, actual outcomes may be different than expected and could have a material effect on our results of operations or cash flows in a particular period.

**Item 1A. Risk Factors**

There have been no material changes to the factors disclosed in Item 1A. Risk Factors in our Annual Report on Form 10-K for the year ended December 31, 2010.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

None.

**Item 3. Defaults Upon Senior Securities**

Not applicable.

**Item 4. Reserved**

**Item 5. Other Information**

None.

**Item 6. Exhibits**

<u>Exhibit No.</u>	<u>Description</u>
31.1	Rule 13a-14(a)/15d-14(a) Certification of Pregis Holding II Corporation's Chief Executive Officer.
31.2	Rule 13a-14(a)/15d-14(a) Certification of Pregis Holding II Corporation's Chief Financial Officer.

**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.

PREGIS HOLDING II CORPORATION

Date: May 11, 2011

By: /s/ D. Keith LaVanway  
D. Keith LaVanway  
Chief Financial Officer (principal financial  
officer and principal accounting officer)

**CERTIFICATION OF CHIEF EXECUTIVE OFFICER  
PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Glenn Fischer, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q for the period ended March 31, 2011 of Pregis Holding II Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations, and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (c) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the board of directors:
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 11, 2011

/s/ Glenn Fischer

Name: Glenn Fischer

Title: President and Chief Executive Officer

**CERTIFICATION OF CHIEF FINANCIAL OFFICER  
PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, D. Keith LaVanway, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q for the period ended March 31, 2011 of Pregis Holding II Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations, and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (c) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the board of directors:
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 11, 2011

/s/ D. Keith LaVanway

Name: D. Keith LaVanway