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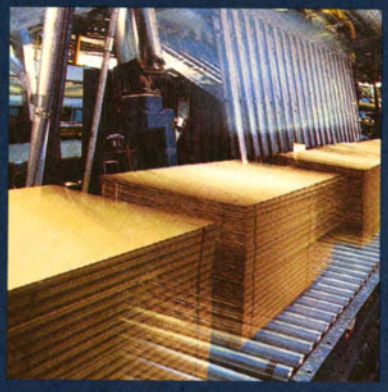
Temple-Inland



# FOCUSED ON THE FUTURE

*Temple-Inland 2007 Annual Report*



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## FINANCIAL HIGHLIGHTS
(In millions, except per share data)

| | 2007 | 2006 |
|---|---|---|
| Revenues | $ 3,926 | $ 4,185 |
| Net income* | $ 1,305 | $ 468 |
| Net income per diluted share* | $ 12.08 | $ 4.22 |
| Dividends per share** | $ 11.37 | $ 1.00 |
| Weighted average diluted shares outstanding | 108.1 | 110.8 |
| Common shares outstanding at year-end | 106.1 | 104.9 |

* Includes one-time after-tax gain on sale of the timberlands for $1,265 or $11.69 per diluted share in 2007
** Includes a $10.25 special dividend in 2007

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**SELECTED BUSINESS SEGMENT DATA**
(In millions)

| | 2007 | 2006 |
|---|---|---|
| *Revenues* | | |
| Corrugated Packaging | $ 3,044 | $ 2,977 |
| Building Products | $ 806 | $ 1,119 |
| Timber and Timberlands* | $ 76 | $ 89 |
| Total | $ 3,926 | $ 4,185 |
| *Segment Operating Income* | | |
| Corrugated Packaging | $ 287 | $ 255 |
| Building Products | $ 8 | $ 221 |
| Timber and Timberlands | $ 65 | $ 63 |
| Total | $ 360 | $ 539 |

* The timberlands were sold on October 31, 2007. This segment will not have revenue or operating income going forward

This annual report contains "forward-looking statements" within the meaning of the federal securities laws. These statements reflect management's current views with respect to future events and are subject to risk and uncertainties. We note that a variety of factors and uncertainties could cause our actual results to differ significantly from the results discussed in the forward-looking statements. Factors and uncertainties that might cause such differences include, but are not limited to: general economic, market, or business conditions; the opportunities (or lack thereof) that may be presented to us and that we may pursue; fluctuations in costs and expenses including the costs of raw materials, purchased energy, and freight; demand for new housing; accuracy of accounting assumptions related to impaired assets, pension and postretirement costs, and contingency reserves; competitive actions by other companies; changes in laws or regulations and actions or restrictions of regulatory agencies; our ability to execute certain strategic and business improvement initiatives; and other factors, many of which are beyond our control.

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# Doyle Simons
# Chairman of the Board and CEO







Welcome to the new Temple-Inland. I am Doyle Simons, your Chairman of the Board and CEO. I, our management team and our 12,000 employees are excited about the future of our company and the opportunity to continue to create value for you, our shareholders. But before I discuss the new Temple-Inland, let me summarize our significant accomplishments in 2007.

Under the leadership of Kenny Jastrow, who retired from our company on December 28, 2007, your Board of Directors announced a Transformation Plan to maximize shareholder value by separating Temple-Inland into three focused, stand-alone public companies and selling our timberlands and returning a majority of the proceeds to shareholders. In fourth quarter 2007, we sold our strategic timberlands for $2.4 billion and paid a $10.25 special dividend to shareholders. On December 28, 2007, we spun off our financial services operation, Guaranty Financial Group, and our real estate operation, Forestar Real Estate Group. Each of the three companies, Temple-Inland, Guaranty Financial Group and Forestar Real Estate Group is well positioned in the marketplace with an appropriate capital structure and greater strategic focus. On behalf of your Board and our employees, we want to thank Kenny for his vision, strategy and leadership over his 29 years of outstanding service, which helped drive our success.

Now to the future. We are committed to making the new Temple-Inland the best and continuing to create value for shareholders, customers and employees. Let me tell you about our company and why we are excited about the future.

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Guaranty FINANCIAL GROUP INC.

FORESTAR Real Estate Group

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# The New Temple-Inland



***Low-Cost, Highly Efficient Manufacturing Company*** The "new" Temple-Inland is a low-cost, highly efficient manufacturing company focused on corrugated packaging and building products. Today we are the third-largest manufacturer of corrugated packaging in North America, producing 3.4 million tons of boxes annually. The corrugated packaging industry has fundamentally changed and we believe it is the best-positioned paper grade. Significant capacity has been taken out of the market resulting in high operating rates, inventories are at historic lows, and pricing for both containerboard and boxes is improving.

In building products, we are a low-cost producer of a tailored portfolio of building products for new home, repair and remodel, and commercial markets. While building products markets are currently challenged, this business has historically been an excellent performer and we believe the long-term industry fundamentals for this business are compelling.

***Committed to Two Key Objectives: (1) Maximizing ROI and (2) Profitably Growing Our Business*** Our two key objectives at Temple-Inland are maximizing return on investment (ROI) and profitably growing our business. We will focus on maximizing ROI because we fundamentally believe there is a direct correlation between ROI and shareholder value. We define ROI very simply: earnings before interest and taxes (EBIT) divided by investment (assets minus current liabilities). We will also look for opportunities to profitably grow our business because we have demonstrated our ability to drive ROI and believe we can create additional value for shareholders through disciplined growth focused on ROI.

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## OUR KEY OBJECTIVES

*At Temple-Inland, we are committed to Maximizing ROI and profitably Growing our business.*



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# Driving ROI through Execution of Strategic Initiatives





***Corrugated Packaging*** By lowering operating costs and maximizing asset utilization, we have become a leader in the corrugated packaging industry. We will continue to drive value in this business through four key strategic initiatives:

- Maintaining full integration, eliminating the need for market-related downtime
- Driving for low cost through a focus on asset utilization and manufacturing excellence
- Improving mix and margins through sales excellence
- Growing the business organically at existing facilities and through acquisition

As a result of our execution of these four key strategic initiatives, our corrugated packaging operation achieved the second-highest ROI in the industry in 2007 and generated the highest relative improvement in return on assets over the past four years. While we have made significant progress, there is more to come through manufacturing and sales excellence.

From 2003–2006, we drove $225 million of business improvement to the bottom line. With what we have in our plans, both on the sales and manufacturing sides of our business, we will drive at least an additional $100 million to the bottom line by year-end 2009. We realized $37 million in business improvement in 2007.

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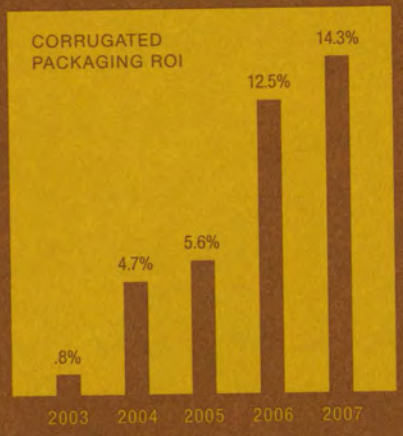




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***Building Products*** In our building products business, we benefit from low-cost, efficient converting operations that are located near large, attractive, high-growth markets. We are focused on four key strategic initiatives:

- Delivering a tailored portfolio of building products designed for new home, repair and remodel, and commercial markets
- Driving low cost through manufacturing excellence and leading-edge technology
- Serving targeted markets with favorable demographics
- Providing sales excellence through unequaled customer service

Even though current markets are challenging, the long-term fundamentals for housing are compelling, driven by favorable demographic trends. We have generated strong ROI from this business and believe that industry fundamentals, coupled with our low-cost system, focus on customers and proximity to large and growing markets, positions us to generate strong ROI going forward.

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80%

of our building products facilities are in the lowest cost quartile.

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GROWING MARKETS

*Our facilities are located near large and growing markets including Houston, Austin, Dallas, San Antonio, Atlanta and the Carolinas.*

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# Foundation for the Future



We used $700 million in proceeds from the sale of our timberlands to pay down debt. As a result, we have a capital structure that allows us to pursue our objectives of maximizing ROI and profitably growing our business.

In terms of our financial priorities, our board declared a quarterly dividend of 10 cents per share in February 2008. In addition, we will continue to look to invest in our business through capital expenditures on a disciplined ROI basis. Our financial priorities also include profitable growth and returning cash to shareholders through share repurchases and dividend increases.

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28%

is our long-term debt to enterprise value ratio.

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## PRIORITIES

- *Investment in our business*
  - *ROI discipline*
- *Profitable growth*
  - *Organic*
  - *Acquisition*
- *Return cash to shareholders*
  - *Dividends*
  - *Share repurchases*

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# Staying True to Our Core Values



While much has changed at Temple-Inland, some things are not changing. Our vision, mission and values have served us well and will continue to provide us with a roadmap of where we are going, how we are going to get there and, most important, our guiding principles along the way. And while we will be passionate about winning, we will win the right way. We will not cut corners, morally, ethically or legally. Integrity matters – to everyone at Temple-Inland.

***Committed to Being the Best*** At Temple-Inland, we have outstanding employees and dedicated leadership committed to being the best. Our ability to win and consistently outperform our competitors depends entirely on the skills, experiences, expertise and commitment of every one of our employees. It is their dedication to hard work and being the best that makes Temple-Inland successful.

Pat Maley was named President and Chief Operating Officer as part of the Transformation Plan. Pat has been instrumental in making us a leader in the corrugated packaging industry. I look forward to working closely with Pat to continue to drive value for shareholders, employees and customers.

Finally, to you our shareholders, thank you for your support. We are committed to maximizing shareholder value and are focused on the future.

Doyle R. Simons

**Doyle R. Simons**
Chairman of the Board and CEO

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## VISION

*Working together to create superior and sustainable value for shareholders, customers and employees.*

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## MISSION

*To be the best by consistently exceeding customer expectations, maximizing asset utilization, lowering costs and improving efficiency.*

## VALUES

*Our customers, our employees, operational efficiency and corporate citizenship.*

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## TEMPLE-INLAND INC. BOARD OF DIRECTORS

PHOTO TOP ROW:

*Donald M. Carlton*
*W. Allen Reed*
*Jeffrey M. Heller*
*Larry R. Faulkner*
*Arthur Temple III*
*Richard M. Smith*

PHOTO BOTTOM ROW:

*E. Linn Draper, Jr.*
*Afsaneh M. Beschloss*
*Doyle R. Simons*
*J. Patrick Maley III*
*Cassandra C. Carr*
*Larry E. Temple*
*James T. Hackett*

## TEMPLE-INLAND INC. EXECUTIVE OFFICERS

**Doyle R. Simons**
*Chairman and Chief Executive Officer*

**J. Patrick Maley III**
*President and Chief Operating Officer*

**Bart J. Doney**
*Group Vice President*

**Jack C. Sweeny**
*Group Vice President*

**Dennis J. Vesci**
*Group Vice President*

**Grant F. Adamson**
*Chief Governance Officer*

**J. Bradley Johnston**
*Chief Administrative Officer*

**Randall D. Levy**
*Chief Financial Officer*

**Scott Smith**
*Chief Information Officer*

**Leslie K. O'Neal**
*Vice President, Assistant General Counsel and Secretary*

**Carolyn C. Sloan**
*Vice President, Internal Audit*

**C. Morris Davis**
*General Counsel*

**Troy L. Hester**
*Principal Accounting Officer and Corporate Controller*

**David W. Turpin**
*Treasurer*

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

# FORM 10-K

(Mark One)

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

**For the Fiscal Year Ended December 29, 2007**

or

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

**For the Transition Period From to**

**Commission File Number 001-08634**

# Temple-Inland Inc.

*(Exact Name of Registrant as Specified in its Charter)*

| **Delaware** | **75-1903917** |
|---|---|
| *(State or Other Jurisdiction of Incorporation or Organization)* | *(I.R.S. Employer Identification No.)* |

**1300 MoPac Expressway South, 3rd Floor**
**Austin, Texas 78746**
*(Address of principal executive offices, including Zip code)*

**Registrant's telephone number, including area code: (512) 434-5800**

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

| Title of Each Class | Name of Each Exchange On Which Registered |
|---|---|
| Common Stock, $1.00 Par Value per Share, non-cumulative | New York Stock Exchange |
| Preferred Share Purchase Rights | New York Stock Exchange |

Securities registered pursuant to Section 12(g) of the Act: None

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**Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ☑ No ☐**

**Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Securities Exchange Act of 1934. Yes ☐ No ☑**

**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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ☑**

**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 Act). Yes ☐ No ☑**

The aggregate market value of the Common Stock held by non-affiliates of the registrant, based on the closing sales price of the Common Stock on the New York Stock Exchange on June 29, 2007, was approximately $5,098,255,000. For purposes of this computation, all officers, directors, and five percent beneficial owners of the registrant (as indicated in Item 12) are deemed to be affiliates. Such determination should not be deemed an admission that such directors, officers, or five percent beneficial owners are, in fact, affiliates of the registrant.

As of February 22, 2008, there were 106,274,170 shares of Common Stock outstanding.

## DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Company's definitive proxy statement to be prepared in connection with the 2008 Annual Meeting of Shareholders are incorporated by reference into Part III of this report.

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secured by irrevocable standby letters of credit. In December 2007, we pledged the notes as collateral for nonrecourse loans. The net cash proceeds from the nonrecourse loans, after current taxes and transaction costs, were approximately $1.8 billion. We used these proceeds to pay a special dividend to our shareholders of $10.25 per share and reduce debt by approximately $700 million.

**Narrative Description of the Business**

*Corrugated Packaging.* Our corrugated packaging segment provided 77.5 percent of our 2007 consolidated net revenues. Our vertically integrated corrugated packaging operation includes:

- five linerboard mills,
- one corrugating medium mill, and
- 64 converting facilities.

We manufacture containerboard and convert it into a complete line of corrugated packaging. We sold eight percent of the containerboard we produced in 2007 in the domestic and export markets. We converted the remaining internal production, in combination with containerboard we purchased from other producers, into corrugated containers at our converting facilities. While we have the capacity to convert more containerboard than we produce, we routinely buy and sell various grades of containerboard depending on our product mix.

Our nationwide network of converting facilities produces a wide range of products from commodity brown boxes to intricate die cut containers that can be printed with multi-color graphics. Even though the corrugated packaging business is characterized by commodity pricing, each order for each customer is a custom order. Our corrugated packaging is sold to a variety of customers in the food, paper, glass containers, chemical, appliance, and plastics industries, among others. We also manufacture bulk containers constructed of multi-wall corrugated board for extra strength, which are used for bulk shipments of various materials.

We serve over 9,500 corrugated packaging customers with 17,000 shipping destinations. We have no single customer to which sales equal ten percent or more of consolidated revenues or the loss of which would have a material adverse effect on our corrugated packaging segment.

Sales of corrugated packaging track changing population patterns and other demographics. Historically, there has been a correlation between the demand for corrugated packaging and orders for nondurable goods.

We also own a 50 percent interest in Premier Boxboard Limited LLC, a joint venture that produces lightweight gypsum facing paper and corrugating medium at a mill in Newport, Indiana.

*Building Products.* Our building products segment provided 20.5 percent of our 2007 consolidated net revenues. We manufacture a wide range of building products, including:

- lumber,
- gypsum wallboard,
- particleboard,
- medium density fiberboard (or MDF), and
- fiberboard.

We sell building products throughout the continental United States, with the majority of sales occurring in the southern United States. We have no single customer to which sales equal ten percent or more of consolidated revenues or the loss of which would have a material adverse effect on our building products segment. Most of our products are sold by account managers and representatives to distributors, retailers, and original equipment manufacturers. Sales of building products are heavily dependent upon the level of residential housing expenditures, including the repair and remodeling market.

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We also own a 50 percent interest in Del-Tin Fiber LLC, a joint venture that produces MDF at a facility in El Dorado, Arkansas.

**Raw Materials**

Wood fiber, in various forms, is the principal raw material we use in manufacturing our products. In October 2007, in conjunction with our transformation plan, we sold our 1.5 million acres of strategic timberland and entered into long-term fiber supply agreements with the purchaser. During 2007, owned timberland supplied approximately 41 percent of our virgin wood fiber requirements. The balance of our virgin wood fiber requirements was purchased from numerous landowners and other timber owners, as well as other producers of wood by-products. In 2008, we currently expect that we will purchase at market prices approximately 50 percent of our wood fiber requirements under our long-term fiber supply agreements, the most significant of which were entered into in connection with our timberland sale. The remainder of our virgin wood fiber requirements will be purchased at market prices from numerous landowners and other timber owners, as well as other producers of wood by-products.

Linerboard and corrugating medium are the principal materials used to make corrugated boxes. Our mills at Rome, Georgia and Bogalusa, Louisiana, only manufacture linerboard. Our Ontario, California; Maysville, Kentucky; and Orange, Texas, mills are traditionally linerboard mills, but can also manufacture corrugating medium. Our New Johnsonville, Tennessee, mill only manufactures corrugating medium. The principal raw material used by the Rome, Georgia; Orange, Texas; and Bogalusa, Louisiana, mills is virgin wood fiber, but each mill is also able to use recycled fiber for up to 15 percent of its wood fiber requirements. The Ontario, California, and Maysville, Kentucky, mills use only recycled fiber. The mill at New Johnsonville, Tennessee, uses a combination of virgin wood and recycled fiber.

In 2007, recycled fiber represented approximately 36 percent of the total wood fiber needs of our containerboard operations. We purchase recycled fiber at market prices on the open market from numerous suppliers. We generally produce more linerboard and less corrugating medium than is used by our converting facilities. The deficit of corrugating medium is filled through open market purchases and/or trades, and we sell any excess linerboard in the open market.

We obtain gypsum for our wallboard operations in Fletcher, Oklahoma, from one outside source through a long-term purchase contract at market prices. At our gypsum wallboard plants in West Memphis, Arkansas, and Cumberland City, Tennessee, synthetic gypsum is used as a raw material. Synthetic gypsum is a by-product of coal-burning electrical power plants. We have a long-term supply agreement for synthetic gypsum produced at a Tennessee Valley Authority electrical plant located adjacent to our Cumberland City plant. Synthetic gypsum acquired pursuant to this agreement supplies all the synthetic gypsum required by our Cumberland City and West Memphis plants. In 2007, our gypsum wallboard plant in McQueeney, Texas, primarily used gypsum obtained from its own quarry and gypsum acquired from the same source that supplies the Fletcher, Oklahoma, plant. In 2008, we expect the McQueeney plant will use synthetic gypsum and gypsum from our quarry.

We believe the sources outlined above will be sufficient to supply our raw material needs for the foreseeable future. We hedge very little of our raw material costs. The wood fiber market is difficult to predict and there can be no assurance of the future direction of prices for virgin wood or recycled fiber. Future increases in wood fiber prices could adversely affect our results of operations.

**Energy**

Electricity and steam requirements at our manufacturing facilities are either supplied by a local utility or generated internally through the use of a variety of fuels, including natural gas, fuel oil, coal, petroleum coke, tire derived fuel, wood bark, and other waste products resulting from the manufacturing process. By utilizing these waste products and other wood by-products as a biomass fuel to generate electricity and steam, we were able to generate approximately 84 percent of our energy requirements in 2007 at our mills in Rome, Georgia; Bogalusa, Louisiana; and Orange, Texas. In some cases where natural gas or fuel oil is used, our facilities possess a dual capacity enabling the use of either fuel as a source of energy.

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In addition to these capital expenditures, we spend a significant amount on ongoing maintenance costs to continue compliance with environmental regulations. We do not believe, however, that these capital expenditures or maintenance costs will have a material adverse effect on our earnings. In addition, expenditures for environmental compliance should not have a material effect on our competitive position because our competitors are also subject to these regulations.

Our facilities are periodically inspected by environmental authorities. We are required to file with these authorities periodic reports on the discharge of pollutants. Occasionally, one or more of these facilities may operate in violation of applicable pollution control standards, which could subject the company to fines or penalties. We believe that any fines or penalties that may be imposed as a result of these violations will not have a material adverse effect on our earnings or competitive position. No assurance can be given, however, that any fines levied in the future for any such violations will not be material.

Under CERCLA, liability for the cleanup of a Superfund site may be imposed on waste generators, site owners and operators, and others regardless of fault or the legality of the original waste disposal activity. While joint and several liability is authorized under CERCLA, as a practical matter, the cost of cleanup is generally allocated among the many waste generators. We are named as a potentially responsible party in five proceedings relating to the cleanup of hazardous waste sites under CERCLA and similar state laws, excluding sites for which our records disclose no involvement or for which our potential liability has been finally determined. In all but one of these sites, we are either designated as a de minimus potentially responsible party or believe our financial exposure is insignificant. We have conducted investigations of all five sites, and currently estimate that the remediation costs to be allocated to us are about $2 million and should not have a material effect on our earnings or competitive position. There can be no assurance that we will not be named as a potentially responsible party at additional Superfund sites in the future or that the costs associated with the remediation of those sites would not be material.

**Competition**

We operate in highly competitive industries. The commodity nature of our manufactured products gives us little control over market pricing or market demand for our products. The level of competition in a given product or market may be affected by economic factors, including interest rates, housing starts, home repair and remodeling activities, and the strength of the dollar, as well as other market factors including supply and demand for these products, geographic location, and the operating efficiencies of competitors. Our competitive position is influenced by varying factors depending on the characteristics of the products involved. The primary factors are product quality and performance, price, service, and product innovation.

The corrugated packaging industry is highly competitive with over 1,350 box plants in the United States. Our box plants accounted for approximately 12.5 percent of total industry shipments in 2007, making us the third largest producer of corrugated packaging in the United States. Although corrugated packaging is dominant in the national distribution process, our products also compete with various other packaging materials, including products made of paper, plastics, wood, and metals.

In building products markets, we compete with many companies that are substantially larger and have greater resources in the manufacturing of building products.

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**Executive Officers of the Registrant**

The names, ages, and titles of our executive officers are:

| Name | Age | Office |
|---|---|---|
| Doyle R. Simons | 44 | Chairman of the Board and Chief Executive Officer |
| J. Patrick Maley III | 46 | President and Chief Operating Officer |
| Bart J. Doney | 58 | Group Vice President |
| Jack C. Sweeny | 61 | Group Vice President |
| Dennis J. Vesci | 60 | Group Vice President |
| Grant F. Adamson | 49 | Chief Governance Officer |
| J. Bradley Johnston | 52 | Chief Administrative Officer |
| Randall D. Levy | 56 | Chief Financial Officer |
| Scott Smith | 53 | Chief Information Officer |
| Leslie K. O'Neal | 52 | Vice President, Assistant General Counsel and Secretary |
| Carolyn C. Sloan | 47 | Vice President, Internal Audit |
| C. Morris Davis | 65 | General Counsel |
| Troy L. Hester | 51 | Principal Accounting Officer and Corporate Controller |
| David W. Turpin | 57 | Treasurer |

Doyle R. Simons became Chairman of the Board and Chief Executive Officer on December 29, 2007. He was previously named Executive Vice President in February 2005 following his service as Chief Administrative Officer since November 2003. Since joining the Company in 1992, Mr. Simons has served as Vice President, Administration from November 2000 to November 2003 and Director of Investor Relations from 1994 through 2000.

J. Patrick Maley III became President and Chief Operating Officer on December 29, 2007. He was previously named Executive Vice President — Paper in November 2004 following his appointment as Group Vice President in May 2003. Prior to joining the Company, Mr. Maley served in various capacities from 1992 to 2003 at International Paper.

Bart J. Doney became Group Vice President in February 2000. Mr. Doney has served as an officer of our corrugated packaging segment since 1990.

Jack C. Sweeny became Group Vice President in May 1996. Since November 1982, Mr. Sweeny has served in various capacities in our building products segment.

Dennis J. Vesci became Group Vice President in August 2005. Mr. Vesci has served as an officer of our corrugated packaging segment since 1998.

Grant F. Adamson became Chief Governance Officer in May 2006. Mr. Adamson joined the Company in 1991 and has served in various capacities including Assistant General Counsel.

J. Bradley Johnston became Chief Administrative Officer in February 2005. Prior to that, Mr. Johnston served as General Counsel from August 2002 through May 2006 and in various capacities in our former financial services segment since 1993.

Randall D. Levy became Chief Financial Officer in May 1999. Mr. Levy joined the Company in 1989 serving in various capacities in our former financial services segment before being named Chief Financial Officer.

Scott Smith became Chief Information Officer in February 2000. Prior to that, Mr. Smith served in various capacities within our former financial services segment since 1988.

Leslie K. O'Neal was named Vice President in August 2002 and became Secretary in February 2000 after serving as Assistant Secretary since 1995. Ms. O'Neal also serves as Assistant General Counsel, a position she has held since 1985.

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certain estimates of expenditures we expect to make for environmental compliance in the next few years. However, we could incur additional significant expenditures due to changes in law or the discovery of new information, and such expenditures could have a material adverse effect on our financial condition, cash flows, and results of operations.

***Downward changes in demand for housing in the market regions where we operate could decrease profitability in our building products segment.***

The residential homebuilding industry is sensitive to changes in economic conditions, including interest rates and availability of financing. Adverse changes in these conditions generally, or in the market regions where we operate, could decrease demand for new homes in these areas. Decline in housing demand could have a negative effect on the pricing and demand for many of our building products, particularly lumber and gypsum wallboard, which could result in a decrease in our revenues and earnings.

***If certain internal restructuring transactions and the distributions of Forestar and Guaranty are determined to be taxable for U.S. federal income tax purposes, we and our stockholders that are subject to U.S. federal income tax could incur significant U.S. federal income tax liabilities.***

We entered into certain internal restructuring transactions in preparation for the spin-offs of Forestar and Guaranty. These transactions are complex and could cause us to incur significant tax liabilities. We received a private letter ruling from the IRS and opinions of tax counsel regarding the tax-free nature of these transactions and the distributions. The ruling and opinions rely on certain facts, assumptions, representations, and undertakings, from us regarding the past and future conduct of our businesses and other matters. If any of these are incorrect or not otherwise satisfied, then we and our stockholders may not be able to rely on the ruling or opinions and could be subject to significant tax liabilities. Notwithstanding the ruling and opinions, the IRS could determine on audit that the distributions or the internal restructuring transactions should be treated as taxable transactions if it determines that any of these facts, assumptions, representations, or undertakings are not correct or have been violated, or if the distributions should become taxable for other reasons, including as a result of significant changes in stock ownership after the distribution.

***If the sale of our strategic timberland did not qualify for installment method reporting for U.S. federal income tax purposes, we could incur significant U.S. federal income tax liabilities the payment of which we believe to be deferred.***

We sold our strategic timberland in a manner intended for U.S. federal income tax purposes to defer recognition of a substantial portion of the gain on the sale. Under the installment method, we will not be required to pay U.S. federal income taxes on the deferred gain until we are required to recognize the gain. We received opinions of tax counsel regarding the timberland sale and the deferred gain. The opinions rely on certain facts, assumptions, representations, and undertakings from us regarding the past and future conduct of our businesses and other matters. If any of these are incorrect or not otherwise satisfied, then we may not be able to rely on the opinions. Notwithstanding the opinions, the IRS could determine on audit that the gain does not qualify for deferral if it determines that any of these facts, assumptions, representations, or undertakings are not correct or have been violated or that the transaction otherwise does not qualify for the installment method.

***We have interest rate risk in connection with our financial assets and nonrecourse financial liabilities of special purpose entities.***

In October 2007, we received $2.38 billion in notes due in 2027 from the sale of our timberland, which we later contributed to two wholly-owned, bankruptcy-remote special purpose entities. In December 2007, the special purpose entities pledged the notes as collateral for $2.14 billion nonrecourse loans payable in 2027. Both the notes and the borrowings require quarterly interest payments based on variable interest rates that reset quarterly. Because of the differences in references rates, margins, and reset dates, there could be periods in which the interest paid on the nonrecourse financial liabilities is significantly more than the interested received on the financial assets.

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## Item 1B. *Unresolved Staff Comments*

None.

## Item 2. *Properties*

We own and operate manufacturing facilities throughout the United States, four converting plants in Mexico, and one in Puerto Rico. We believe our manufacturing facilities are suitable for their purposes and adequate for our business. Additional information about selected facilities by business segment follows:

**Containerboard Mills**

| Location | Product | Number of Machines | Annual Capacity | 2007 Production |
|---|---|---|---|---|
| | | | (In tons) | |
| Ontario, California | Linerboard and corrugating medium | 1 | 336,000 | 334,479 |
| Rome, Georgia | Linerboard | 2 | 837,000 | 834,069 |
| Orange, Texas | Linerboard and corrugating medium | 2 | 730,000 | 725,546 |
| Bogalusa, Louisiana | Linerboard | 2 | 915,000 | 916,021 |
| Maysville, Kentucky | Linerboard and corrugating medium | 1 | 454,000 | 455,102 |
| New Johnsonville, Tennessee | Corrugating medium | 1 | 348,000 | 349,706 |
| | | | 3,620,000 | 3,614,923 |
| Newport, Indiana* | Corrugating medium, linerboard, and gypsum facing paper | 1 | 308,000 | 300,882 |

* The table shows the full capacity of this facility that is owned by a joint venture in which we own a 50 percent interest. In 2007, we purchased 52,788 tons of corrugating medium and linerboard and 42,136 tons of gypsum facing paper from the venture.

**Converting Facilities***

| Location | Corrugator Size |
|---|---|
| Phoenix, Arizona | 98″ |
| Fort Smith, Arkansas | 87″ |
| Fort Smith, Arkansas[(1)]*** | None |
| Bell, California | 98″ |
| Buena Park, California[(1)] | 85″ |
| El Centro, California[(1)] | 87″ |
| Gilroy, California[(1)] | 87″ |
| Gilroy, California[(1)]*** | 98″ |
| Ontario, California | 87″ |
| Santa Fe Springs, California | 98″ |
| Santa Fe Springs, California[(1)]** | 87″ and 85″ |
| Santa Fe Springs, California[(1)]*** | None |
| Tracy, California | 110″ |
| Union City, California[(1)]*** | None |
| Wheat Ridge, Colorado | 87″ |
| Orlando, Florida | 98″ |
| Tampa, Florida[(1)] | 78″ |
| Rome, Georgia | 98″ |
| Carol Stream, Illinois | 87″ |
| Chicago, Illinois | 87″ |

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### Other

We occupy approximately 190,000 square feet of leased office space in Austin, Texas. We own and occupy a 150,000 square feet office building in Diboll, Texas.

At year-end 2007, property and equipment having a net book value of $2 million were subject to liens in connection with $14 million of debt.

## Item 3. *Legal Proceedings*

### General

We are involved in various legal proceedings that arise from time to time in the ordinary course of doing business. We believe that adequate reserves have been established for any probable losses and that the outcome of any of these proceedings should not have a material adverse effect on our financial position or long-term results of operations or cash flows. It is possible, however, that charges related to these matters could be significant to results of operations or cash flows in any single accounting period. A summary of our more significant legal matters is set forth below.

### Antitrust Litigation

On May 14, 1999, we and eight other linerboard manufacturers were named as defendants in a consolidated class action complaint that alleged a civil violation of Section 1 of the Sherman Act. In addition, complaints containing allegations similar to those in the class action were filed by certain opt-out plaintiffs. Over the last several years, we have paid a total of $13 million to settle the class action and a majority of the opt-out claims. In December 2007, we agreed to participate in binding arbitration in an effort to resolve most of the remaining claims. As a result of the arbitration, we paid $48 million on the claims submitted to arbitration and to settle all remaining opt-out claims in the federal litigation.

One related Kansas state court claim for approximately $26 million in statutory damages, which could be trebled under applicable state law, is still pending against us.

### Bogalusa Litigation

On October 15, 2003, a release of nitrogen dioxide and nitrogen oxide took place at our linerboard mill in Bogalusa, Louisiana. The mill followed appropriate protocols for handling this type of event, notifying the Louisiana Department of Environmental Quality, the U.S. Environmental Protection Agency, and local law enforcement officials. The federal and state environmental agencies have analyzed the reports we prepared and have not indicated that they will take any action against us.

To date, we have been served with 11 lawsuits seeking damages for various personal injuries allegedly caused by either exposure to the released gas or fears of exposure. These 11 lawsuits have been consolidated under Louisiana state rules for purpose of discovery and are set for trial in third quarter 2008. We are vigorously defending against these allegations.

### Asbestos

We are a defendant in various lawsuits involving alleged workplace exposure to asbestos. These cases involve exposure to asbestos in premises owned or operated by us. We do not manufacture any products that contain asbestos and all our cases in this area are limited to workplace exposure claims. Historically, our aggregate annual settlements related to asbestos claims have been approximately $1 million. The number of claims has remained relatively constant in the past few years despite the fact that the majority of the claims relate to a facility we sold at the end of 1999.

### Other

We are also defending two cases in California state court alleging violations of that state's on-duty meal break laws. In 2007, we settled three additional meal break cases.

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## Item 4. *Submission of Matters to a Vote of Security Holders*

We did not submit any matter to a vote of our shareholders in fourth quarter 2007.

## PART II

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

### Market Information

Our Common Stock is traded on the New York Stock Exchange. The high and low sales prices for our Common Stock and dividends paid in each fiscal quarter in the two most recent fiscal years were:

| | 2007 | | | 2006 | | |
|---|---|---|---|---|---|---|
| | Price Range | | | Price Range | | |
| | High | Low | Dividends | High | Low | Dividends |
| First Quarter | $63.61 | $44.29 | $ 0.28 | $47.92 | $40.83 | $0.25 |
| Second Quarter | $64.45 | $59.00 | $ 0.28 | $47.68 | $38.12 | $0.25 |
| Third Quarter | $66.28 | $49.17 | $ 0.28 | $45.48 | $39.78 | $0.25 |
| Fourth Quarter* | $57.51 | $29.09 | $10.53 | $46.71 | $37.84 | $0.25 |
| For the Year | $66.28 | $29.09 | $11.37 | $47.92 | $37.84 | $1.00 |

* Includes a special dividend of $10.25 per share paid in December 2007.

### Shareholders

Our stock transfer records indicated that as of February 22, 2008, there were approximately 4,750 holders of record of our Common Stock.

### Dividend Policy

As indicated above, we paid quarterly dividends during each of the two most recent years in the amounts shown. In addition to our regular quarterly dividend, we paid a special dividend of $10.25 per share in December 2007 as part of our transformation plan. On February 1, 2008, the Board of Directors declared a quarterly dividend on our Common Stock of $0.10 per share payable on March 14, 2008, to shareholders of record on February 29, 2008. The Board periodically reviews the dividend policy, and the declaration of dividends will necessarily depend upon our earnings and financial requirements and other factors within the discretion of the Board.

### Issuer Purchases of Equity Securities[1]

| Period | Total Number of Shares Purchased | Average Price Paid per Share | Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs | Maximum Number of Shares That May Yet be Purchased Under the Plans or Programs |
|---|---|---|---|---|
| Month 1 (10/1/2007 — 10/31/2007) | — | $— | — | 6,650,000 |
| Month 2 (11/1/2007 — 11/30/2007) | — | $— | — | 6,650,000 |
| Month 3 (12/1/2007 — 12/31/2007) | — | $— | — | 6,650,000 |
| Total | — | $— | — | |

(1) On August 4, 2006, we announced that our Board of Directors authorized the repurchase of up to 6,000,000 shares of our common stock. We have purchased 4,350,000 shares under this authorization, which has no expiration date. On February 2, 2007, we announced that our Board of Directors authorized the

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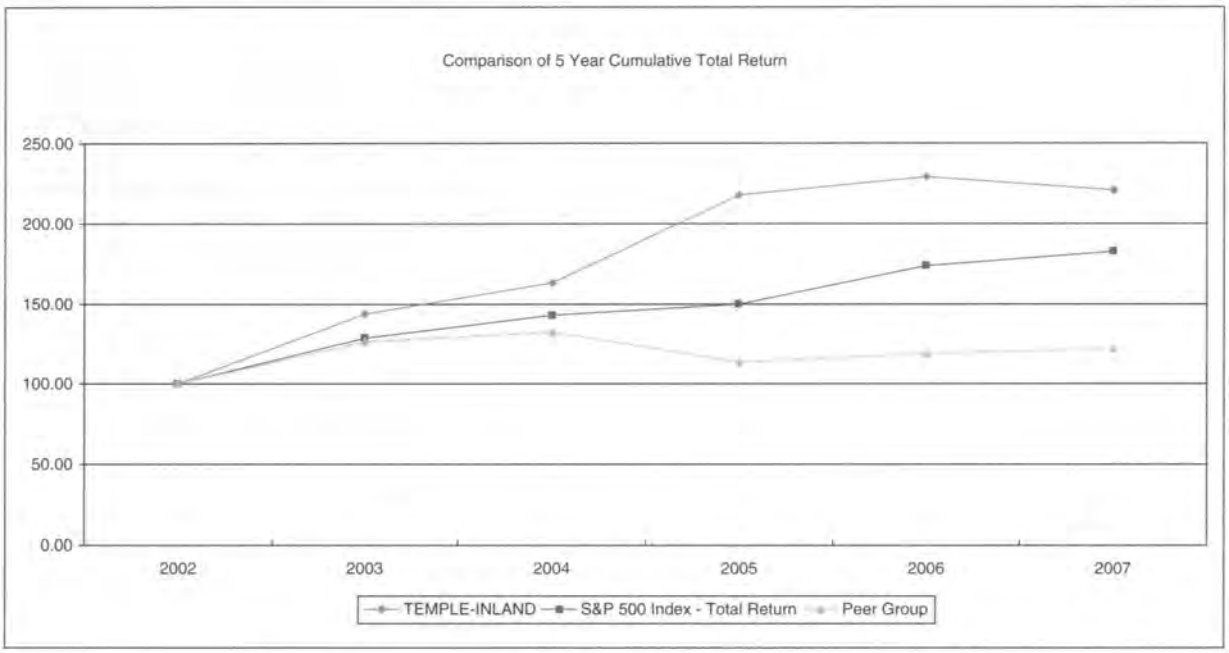
purchase of up to an additional 5,000,000 shares of our common stock, increasing the maximum number of shares yet to be purchased under our repurchase plans to 6,650,000 shares. We have no plans or programs that expired during the period covered by the table above and no plans or programs that we intend to terminate prior to expiration or under which we no longer intend to make further purchases.

**Performance Graph**

We composed an index of our peers consisting of AbitibiBowater Inc., Caraustar Industries, Inc., Domtar Corporation, International Paper Company, MeadWestvaco Corporation, Packaging Corporation of America, Smurfit-Stone Container Corporation, and Weyerhaeuser Corporation (Peer Index). During the five preceding years, our cumulative total stockholder return compared to the Standard & Poor's 500 Stock Index and to the Peer Index was as shown in the following table:




Assumes $100 invested on the last trading day in fiscal year 2002
*Total return assumes reinvestment of dividends

**Other**

**See Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters** for disclosure regarding securities authorized for issuance under equity compensation plans.

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## Item 6. *Selected Financial Data*

| | For the Year | | | | |
|---|---|---|---|---|---|
| | 2007 | 2006[a] | 2005 | 2004 | 2003[b] |
| | (Dollars in millions, except per share) | | | | |
| Revenues: | | | | | |
| Corrugated packaging | $3,044 | $ 2,977 | $ 2,825 | $ 2,736 | $ 2,700 |
| Building products | 806 | 1,119 | 898 | 851 | 684 |
| Timber and timberland | 76 | 89 | 120 | 107 | 108 |
| Total revenues | $3,926 | $ 4,185 | $ 3,843 | $ 3,694 | $ 3,492 |
| Segment operating income: | | | | | |
| Corrugated packaging | $ 287 | $ 255 | $ 120 | $ 96 | $ 18 |
| Building products | 8 | 221 | 125 | 129 | 2 |
| Timber and timberland | 65 | 63 | 72 | 52 | 42 |
| Segment operating income | 360 | 539 | 317 | 277 | 62 |
| Items not allocated to segments: | | | | | |
| General and administrative | (100) | (107) | (91) | (79) | (73) |
| Share-based compensation | (34) | (38) | (21) | (12) | (6) |
| Gain on sale of timberland | 2,053 | — | — | — | — |
| Other operating income (expense)[c] | (188) | 26 | (85) | (42) | (133) |
| Other non-operating income (expense)[c] | (35) | 93 | — | — | (8) |
| Net interest income on financial assets and nonrecourse financial liabilities of special purpose entities[d] | 10 | — | — | — | — |
| Interest expense on debt | (111) | (123) | (109) | (125) | (135) |
| Income (loss) before taxes | 1,955 | 390 | 11 | 19 | (293) |
| Income tax (expense) benefit[e] | (753) | (103) | 7 | 8 | 264 |
| Income from continuing operations | 1,202 | 287 | 18 | 27 | (29) |
| Discontinued operations[f] | 103 | 181 | 158 | 133 | 131 |
| Effect of accounting change[g] | — | — | — | — | (1) |
| Net income | $1,305 | $ 468 | $ 176 | $ 160 | $ 101 |
| Diluted earnings per share: | | | | | |
| Income from continuing operations | $11.12 | $ 2.59 | $ 0.16 | $ 0.24 | $ (0.27) |
| Discontinued operations[f] | 0.96 | 1.63 | 1.38 | 1.18 | 1.21 |
| Effect of accounting change[g] | — | — | — | — | (0.01) |
| Net income | $12.08 | $ 4.22 | $ 1.54 | $ 1.42 | $ 0.93 |
| Dividends per common share[h] | $11.37 | $ 1.00 | $ 0.90 | $ 1.22 | $ 0.68 |
| Average diluted shares outstanding | 108.1 | 110.8 | 114.5 | 112.4 | 108.4 |
| Common shares outstanding at year-end | 106.1 | 104.9 | 111.0 | 112.2 | 109.2 |
| Depreciation and amortization | $ 214 | $ 225 | $ 218 | $ 219 | $ 233 |
| Capital expenditures | $ 237 | $ 204 | $ 220 | $ 219 | $ 134 |
| At Year-End: | | | | | |
| Assets: | | | | | |
| Manufacturing assets | $3,559 | $ 3,627 | $ 3,411 | $ 3,522 | $ 3,474 |
| Financial assets of special purpose entities | 2,383 | — | — | — | — |
| Assets of discontinued operations | — | 16,847 | 18,219 | 16,622 | 17,893 |
| Total assets | $5,942 | $20,474 | $21,630 | $20,144 | $21,367 |
| Debt (long-term excluding current maturities and nonrecourse financial liabilities of special purpose entities) | $ 852 | $ 1,584 | $ 1,498 | $ 1,485 | $ 1,611 |
| Nonrecourse financial liabilities of special purpose entities | $2,140 | $ — | $ — | $ — | $ — |
| Liability for pension and postretirement benefits | $ 256 | $ 366 | $ 407 | $ 432 | $ 396 |
| Shareholders' equity | $ 780 | $ 2,189 | $ 2,080 | $ 2,107 | $ 1,988 |
| Ratio of debt to total capitalization | 52% | 42% | 42% | 41% | 45% |

(a) In January 2006, we purchased our partner's 50 percent interest in Standard Gypsum LP for $150 million and assumed debt of $28 million. Unaudited pro forma information assuming this acquisition and related financing had occurred at the beginning of 2005 follows: revenues $4.04 billion; income from continuing operations $32 million; and income from continuing operations, per diluted share $0.28. These pro forma results are not necessarily an indication of what actually would have occurred if the acquisition and financing transactions had been completed at the beginning of the periods presented and are not intended to be indicative of future results.

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(b) The 2003 fiscal year, which ended on January 3, 2004, had 53 weeks. The extra week did not have a significant effect on earnings or financial position. As a result of the consolidation of our administrative functions and adoption of a shared services concept, beginning 2004, we changed the way we allocate costs to our business segments. The effect of this change was to increase segment operating income and to increase unallocated expenses by a like amount. The 2003 amounts have been reclassified to reflect this change.

(c) Other operating and non-operating income (expense) consists of:

| | For the Year | | | | |
|---|---|---|---|---|---|
| | 2007 | 2006 | 2005 | 2004 | 2003 |
| | (In millions) | | | | |
| Other operating income (expense): | | | | | |
| Transformation costs (advisory and legal fees, change of control and employee related) | $ (69) | $— | $ — | $ — | $ — |
| Closure and sale of converting and production facilities and sale of non-strategic assets | (55) | (4) | (50) | (27) | (83) |
| Litigation | (56) | (6) | (13) | — | — |
| Environmental remediation | (9) | (8) | (3) | — | — |
| Softwood Lumber Agreement | — | 42 | — | — | — |
| Hurricane related costs and, in 2006, related insurance proceeds | — | 2 | (16) | — | — |
| Consolidation of administrative functions | — | — | — | (11) | (48) |
| Other | 1 | — | (3) | (4) | (2) |
| | $(188) | $26 | $(85) | $(42) | $(133) |
| Other non-operating income (expense): | | | | | |
| Charges related to early repayment of debt | $ (40) | $— | $ (6) | $ (2) | $ (8) |
| Tax litigation and other settlements | — | 89 | 2 | — | — |
| Interest and other income | 5 | 4 | 4 | 2 | — |
| | $ (35) | $93 | $ — | $ — | $ (8) |

(d) In October 2007, we received $2.38 billion in notes from the sale of our timberland, which we later contributed to two wholly-owned, bankruptcy-remote special purpose entities. In December 2007, the special purpose entities pledged the notes as collateral for $2.14 billion nonrecourse loans payable in 2027. Both the notes and the borrowings require quarterly interest payments based on variable interest rates that reset quarterly. We include these two special purpose entities in our consolidated financial statements.

(e) Income taxes include one-time tax benefits of: $7 million in 2007, of which $3 million is related to changes to the State of Texas margin tax and $4 million is related to the resolution of state income tax matters; $36 million in 2006, of which $6 million is related to the State of Texas margin tax and $30 million is related to the non-taxable tax litigation settlement; $16 million in 2005 related to the sale of our Pembroke, Canada MDF facility; and $20 million in 2004 and $165 million in 2003 related to the resolution and settlement of prior years' tax examinations.

(f) Discontinued operations include the operations of our financial services and real estate segments, which were spun off to our shareholders on December 28, 2007, and the non-strategic operations obtained in the Gaylord acquisition, including the multi-wall bag business and kraft paper mill which were sold in January 2003 and the chemical business which was sold in August 2007. The resolution and settlement of environmental and other indemnifications we provided in the 1999 sale of the bleached paperboard operation are also included in 2004.

(g) In 2003, we adopted Statement of Financial Accounting Standards (SFAS) No. 143, *Accounting for Asset Retirement Obligations,* which resulted in an after-tax cumulative effect charge of $1 million.

In 2006, (i) we adopted the modified prospective application of SFAS No. 123 (revised December 2004), *Share-Based Payment*, which decreased 2006 income before taxes by $6 million; (ii) we began applying the guidance in Emerging Issues Task Force (EITF) Issue No. 04-13, *Accounting for Purchases and Sales*

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*of Inventory with the Same Counterparty*, which decreased income before taxes by $7 million in 2006 and $2 million in 2007; and (iii) we adopted SFAS No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans*, which increased our liability for pension and postretirement benefits by $76 million, decreased prepaid expenses and other assets by $16 million, decreased deferred income taxes by $35 million, and decreased shareholders' equity by $57 million.

In 2007, (i) we adopted Financial Accounting Standards Board (FASB) Interpretation No. 48 (FIN 48), *Accounting for Uncertainty in Income Taxes*, which increased assets by $2 million, reduced liabilities by $3 million and increased beginning retained earnings by $5 million (we also reclassified $11 million from deferred income taxes to other long-term liabilities), (ii) we adopted the measurement provisions of SFAS No. 158, *Employer's Accounting for Defined Benefit Pension and Other Postretirement Plans*, which reduced beginning retained earnings by $5 million, and (iii) we adopted FASB Staff Position No. AUG AIR-1, *Accounting for Planned Major Maintenance Activities*, electing the expense-as-incurred method which had no effect on our annual earnings or financial position.

(h) Includes special dividends of $10.25 per share in 2007 and $0.50 per share in 2004.

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

### Forward-Looking Statements

Management's Discussion and Analysis of Financial Condition and Results of Operations contains "forward-looking statements" within the meaning of the federal securities laws. These forward-looking statements are identified by their use of terms and phrases such as "believe," "anticipate," "could," "estimate," "likely," "intend," "may," "plan," "expect," and similar expressions, including references to assumptions. These statements reflect management's current views with respect to future events and are subject to risk and uncertainties. We note that a variety of factors and uncertainties could cause our actual results to differ significantly from the results discussed in the forward-looking statements. Factors and uncertainties that might cause such differences include, but are not limited to:

- general economic, market, or business conditions;
- the opportunities (or lack thereof) that may be presented to us and that we may pursue;
- fluctuations in costs and expenses including the costs of raw materials, purchased energy, and freight;
- demand for new housing;
- accuracy of accounting assumptions related to impaired assets, pension and postretirement costs, and contingency reserves;
- competitive actions by other companies;
- changes in laws or regulations;
- our ability to execute certain strategic and business improvement initiatives; and
- other factors, many of which are beyond our control.

Our actual results, performance, or achievement probably will differ from those expressed in, or implied by, these forward-looking statements, and accordingly, we can give no assurances that any of the events anticipated by the forward-looking statements will transpire or occur, or if any of them do so, what impact they will have on our results of operations or financial condition. In view of these uncertainties, you are cautioned not to place undue reliance on these forward-looking statements. Except as required by law, we expressly disclaim any obligation to publicly revise any forward-looking statements contained in this report to reflect the occurrence of events after the date of this report.

### Non-GAAP Financial Measure

Return on investment (ROI) is an important internal measure for us because it is a key component of our evaluation of overall performance and the performance of our business segments. Studies have shown that

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there is a direct correlation between shareholder value and ROI and that shareholder value is created when ROI exceeds the cost of capital. ROI allows us to evaluate our performance on a consistent basis as the amount we earn relative to the amount invested in our business segments. A significant portion of senior management's compensation is based on achieving ROI targets.

In evaluating overall performance, we define ROI as total segment operating income, less general and administrative expenses and share-based compensation not allocated to segments; divided by total assets, less certain assets and certain current liabilities. As a result of our transformation in 2007, we modified the return portion of this calculation. The ROI for all prior years has been recalculated to reflect this change. We do not believe there is a comparable GAAP financial measure to our definition of ROI. The reconciliation of our ROI calculation to amounts reported under GAAP is included in a later section of Management's Discussion and Analysis of Financial Condition and Results of Operations.

Despite its importance to us, ROI is a non-GAAP financial measure that has no standardized definition and as a result may not be comparable with other companies' measures using the same or similar terms. Also there may be limits in the usefulness of ROI to investors. As a result, we encourage you to read our consolidated financial statements in their entirety and not to rely on any single financial measure.

## Accounting Policies

*Critical Accounting Estimates*

In preparing our financial statements, we follow generally accepted accounting principles, which in many cases require us to make assumptions, estimates, and judgments that affect the amounts reported. Our significant accounting policies are included in **Note 1 to the Consolidated Financial Statements.** Many of these principles are relatively straightforward. There are, however, a few accounting policies that are critical because they are important in determining our financial condition and results, and they are difficult for us to apply. They include asset impairments, contingency reserves, and pension accounting. The difficulty in applying these policies arises from the assumptions, estimates and judgments that we have to make currently about matters that are inherently uncertain, such as future economic conditions, operating results and valuations, as well as our intentions. As the difficulty increases, the level of precision decreases, meaning actual results can, and probably will, be different from those currently estimated. We base our assumptions, estimates, and judgments on a combination of historical experiences and other factors that we believe are reasonable. We have discussed the selection and disclosure of these critical accounting estimates with our Audit Committee.

- Measuring assets for impairment requires estimating intentions as to holding periods, future operating cash flows and residual values of the assets under review. Changes in our intentions, market conditions, or operating performance could require us to revise the impairment charges we previously provided.

- The expected long-term rate of return on pension plan assets is an important assumption in determining pension expense. In selecting that rate, currently 6.875 percent, particular consideration is given to our asset allocation because approximately 80 percent of our plan assets are debt related with a duration that closely matches that of our benefit obligation. Another important consideration is the discount rate used to determine the present value of our benefit obligation, currently 6.125 percent. Differences between actual and expected rates of return and changes in the discount rate will affect future pension expense and funded status. For example, a 25 basis point change in the discount rate would affect the projected benefit obligation by about $42 million and the interest cost on the projected benefit obligation by about $5 million. However, due to our move in late 2007 to a more matched position between our plan assets and our projected benefit obligation, we would expect a 25 basis point change in the discount rate to affect the funded status of our plan by only $12 million and the total net periodic benefit expense by only $2 million.

- Contingency reserves are established for potential losses related to litigation, environmental remediation, and disputes with taxing authorities, among other items. Estimating these reserves requires us to make certain judgments and assumptions regarding actual or potential claims, interpretations to be made by courts or

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regulatory bodies, and other factors and events that are outside our control. Changes and inaccuracies in our interpretations and actions of others could require us to revise the reserves we previously provided.

*New Accounting Pronouncements and Change in Measurement Date of our Defined Benefit and Postretirement Plans*

In the last three years, we adopted a number of new accounting pronouncements, including in 2007, FASB Staff Position No. AUG AIR-1, *Accounting for Planned Major Maintenance Activities;* FIN 48, *Accounting for Uncertainty in Income Taxes*; and a fiscal year-end measurement date for valuing plan assets and obligations for our defined benefit and postretirement benefit plans as required by SFAS No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans*. In addition, there are four new accounting pronouncements that we will be required to adopt in 2008 and 2009, none of which we expect to have a significant effect on our financial position, results of operations or cash flows. Please read **Note 1 to the Consolidated Financial Statements** for additional information.

*Transformation*

On December 28, 2007, we completed our transformation plan that was approved by our board of directors in February 2007. A summary of the significant elements of the transformation plan follows:

- On October 31, 2007, we sold 1.55 million acres of timberland for $2.38 billion to an investment entity affiliated with The Campbell Group, LLC and recognized a pre-tax gain of $2.053 billion, which is included in other operating income. The acreage sold consisted of 1.38 million acres owned in fee and leases covering 175,000 acres. The total consideration consisted almost entirely of notes due in 2027 that are secured by irrevocable letters of credit issued by independent financial institutions. We also entered into a 20-year fiber supply agreement for pulpwood and a 12-year fiber supply agreement for sawtimber. Both agreements are at market prices and are subject to extension.
- We contributed the notes and irrevocable letters of credit received in connection with the sale of our timberland to two wholly-owned, bankruptcy-remote special purpose entities. On December 3, 2007, the special purpose entities pledged the notes received from the sale of the timberland as collateral for $2.14 billion nonrecourse loans payable in 2027. The net cash proceeds, after alternative minimum and other taxes related to sale of the timberland and transactions costs, were $1.8 billion. We used $1.1 billion of the net cash proceeds to pay a $10.25 per share special cash dividend to our shareholders in December 2007. The remaining $700 million was used to reduce debt. We have concluded that we are the primary beneficiary of these special purpose entities. As a result, we include these special purpose entities in our consolidated financial statements.
- On December 28, 2007, we completed the spin-off of our real estate segment, Forestar Real Estate Group Inc. (Forestar), and our financial services segment, Guaranty Financial Group Inc. (Guaranty). These spin-offs were effected through tax-free distributions of one share of Forestar and one share of Guaranty for every three shares of Temple-Inland common stock. These spin-offs reduced retained earnings by $1.6 billion. Our financial information has been reclassified to reflect Forestar and Guaranty as discontinued operations for all periods presented.

The transformation plan significantly changed our capital structure and operations. At year-end 2007, Temple-Inland is a manufacturing company focused on corrugated packaging and building products.

## Results of Operations for the Years 2007, 2006, and 2005

### Summary

Our two key objectives are:

- Maximizing ROI and
- Profitably growing our business

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We will accomplish our key objectives through execution of our strategic initiatives. Our key strategic initiatives in corrugated packaging are:

- Maintaining full integration,
- Driving for low cost through asset utilization and manufacturing excellence,
- Improving mix and margins through sales excellence, and
- Growing our business.

Our key strategic initiatives in building products are:

- Delivering a tailored portfolio of building products,
- Driving for low cost through manufacturing excellence,
- Serving growing markets with favorable demographics, and
- Promoting sales excellence.

In 2007, consistent with our key strategic initiatives:

- We had record production in our containerboard mills through manufacturing excellence.
- We continued to drive for low cost.
- We improved asset utilization in our box plants through manufacturing excellence.
- We grew our box shipments by one percent through sales excellence (excluding shipments from Performance Sheets, which was sold in August 2006).

A summary of our consolidated results from continuing operations follows:

| | For the Year | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| | (Dollars in millions, except per share) | | |
| Consolidated revenues | $3,926 | $4,185 | $3,843 |
| Income from continuing operations | 1,202 | 287 | 18 |
| Income from continuing operations, per diluted share | 11.12 | 2.59 | 0.16 |
| ROI | 7.8% | 13.4% | 7.2% |

In 2007, significant items affecting income from continuing operations included:

- In connection with our transformation plan, we recognized a $2.053 billion gain on sale of our strategic timberland, and we incurred $109 million in expenses primarily related to early repayment of debt, change of control agreements and other employee payments, and legal and advisory services.
- We experienced higher prices for our corrugated packaging products; however, we experienced lower prices and volumes for most of our building products.
- While we continue to see the benefit in our manufacturing operations from our initiatives to lower costs, improve asset utilization, and increase operating efficiencies, the higher cost of recycled fiber used at our containerboard mills offset some of the benefits.
- We recognized $120 million in charges, including $64 million as a result of the decision to cease production permanently at our Mt. Jewett particleboard facility and $56 million for the settlement of antitrust and other litigation.

In 2006, significant items affecting income from continuing operations included:

- We continued to see benefits in our manufacturing operations from our initiatives to lower costs, improve asset utilization, and increase operating efficiencies.

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- We experienced improved markets for our corrugated packaging and building products, principally gypsum wallboard and particleboard. We acquired our partner's 50 percent interest in Standard Gypsum LP in January.
- Charges related to facility closures and environmental remediation at a paper mill site totaled $12 million.
- We realized one-time cash gains of $89 million related to the settlement of tax litigation and $42 million related to the Softwood Lumber Agreement entered into between the U.S. and Canada.

In 2005, significant items affecting income from continuing operations included:

- We continued to see benefits in our manufacturing operations from our initiatives to lower costs, improve asset utilization, and increase operating efficiencies.
- Charges related to facility closures were $58 million.
- In connection with the sale of our Canadian MDF facility, we recognized a one-time tax benefit of $16 million.
- Hurricanes Katrina and Rita adversely affected segment operating income by about $11 million due to production downtime and re-start expenses.
- Hurricane related losses and other unusual expenses related to litigation and the early repayment of debt totaled $32 million.

**Business Segments**

As a result of the transformation plan, at year-end 2007, we have two ongoing business segments: corrugated packaging and building products. Timber and timberland, which managed our timber resources, is no longer an active segment as a result of the sale of our timberlands in fourth quarter 2007. Our financial information has been reclassified to reflect the spun-off entities, Forestar and Guaranty, as discontinued operations.

Our operations are affected to varying degrees by supply and demand factors and economic conditions including changes in new housing starts, home repair and remodeling activities, and the strength of the U.S. dollar. Given the commodity nature of our manufactured products, we have little control over market pricing or market demand.

**Corrugated Packaging**

We manufacture linerboard and corrugating medium that we convert into corrugated packaging and sell in the open market. Our corrugated packaging segment revenues are principally derived from the sale of corrugated packaging products and, to a lesser degree, from the sale of linerboard in the domestic and export markets. We also own a 50 percent interest in Premier Boxboard Limited LLC, a joint venture that produces light-weight gypsum facing paper and corrugating medium at a mill in Newport, Indiana.

A summary of our corrugated packaging results follows:

| | For the Year | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| | (Dollars in millions) | | |
| Revenues | $ 3,044 | $ 2,977 | $ 2,825 |
| Costs and expenses | (2,757) | (2,722) | (2,705) |
| Segment operating income | $ 287 | $ 255 | $ 120 |
| Segment ROI | 14.3% | 12.5% | 5.6% |

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Hurricanes Katrina and Rita adversely affected 2005 segment operating results by about $10 million principally related to mill production downtime and re-start expenses at our Bogalusa, Louisiana and Orange, Texas linerboard mills.

Fluctuations in product pricing, which includes freight and is net of discounts, and shipments are set forth below:

| | Year over Year Increase (Decrease) | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| **Corrugated packaging** | | | |
| Average prices | 3% | 6% | 2% |
| Shipments, average week[a] | (1)% | (2)% | 2% |
| Industry shipments, average week[b] | (2)% | 1% | 1% |
| **Linerboard** | | | |
| Average prices | 5% | 22% | (6)% |
| Shipments, in thousand tons | (7) | 46 | (56) |

(a) Excluding the impact of the sale of Performance Sheets in August 2006, our shipments were up one percent in 2007.

(b) Source: Fibre Box Association

In 2007, corrugated packaging prices and linerboard prices moved higher as a result of price increases implemented in 2006 and 2007. In 2006, corrugated packaging and linerboard prices moved higher reflecting price increases implemented in late 2005 and in 2006.

Linerboard shipments to third parties were slightly lower than in 2006. Linerboard shipments and sales to third parties increased in 2006 due to increased mill production.

Costs and expenses were up one percent in 2007 compared with 2006 and up one percent in 2006 compared with 2005. In 2007, higher raw material costs were partially offset by lower pension and postretirement costs, $8 million in business interruption and other insurance proceeds primarily related to an equipment outage and other operational issues at our mills that occurred in 2006, and cost reductions attributable to the sale of Performance Sheets. Increased mill reliability and efficiency resulted in lower maintenance costs and improved raw material yield and energy usage. In 2006, higher wood fiber and freight costs were partially offset by lower recycled fiber, energy, and healthcare costs.

Fluctuations in our significant cost and expense components included:

| | Year over Year Increase (Decrease) | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| | (In millions) | | |
| Wood fiber | $ 8 | $16 | $ 22 |
| Recycled fiber | 77 | (9) | (6) |
| Energy, principally natural gas | (1) | (8) | 30 |
| Freight | (3) | 32 | 40 |
| Depreciation | (11) | (7) | 1 |
| Health care | (1) | (3) | (16) |
| Pension and postretirement | (12) | (2) | (3) |

The costs of our wood and recycled fiber, energy, and freight fluctuate based on the market prices we pay for these commodities. It is likely that these costs will continue to fluctuate in 2008. The decrease in depreciation was principally due to the continued use of fully depreciated assets and the sale of Performance Sheets in August 2006.

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Information about our converting facilities and mills follows:

| | For the Year | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| Number of converting facilities (at year end) | 64 | 64 | 65 |
| Corrugated packaging shipments, in million tons | 3.4 | 3.4 | 3.4 |
| Mill production, in million tons | 3.6 | 3.6 | 3.4 |
| Percent mill production used internally | 92% | 91% | 92% |
| Percent of total fiber requirements sourced from recycled fiber | 36% | 34% | 36% |
| Corrugating medium purchases from our Premier Boxboard Limited LLC joint venture, in thousand tons | 53 | 85 | 68 |

**Building Products**

We manufacture lumber, gypsum wallboard, particleboard, medium density fiberboard (MDF), and fiberboard. Our building products segment revenues are principally derived from sales of these products. We also own a 50 percent interest in Del-Tin Fiber LLC, a joint venture that produces MDF at a facility in El Dorado, Arkansas.

In 2006, we purchased our partner's 50 percent interest in Standard Gypsum LP, a joint venture that produced gypsum wallboard. Results of operations have been consolidated since the date of purchase.

A summary of our building products results follows:

| | For the Year | | | |
|---|---|---|---|---|
| | 2007 | 2006 | 2005 | |
| | Actual | Actual | Actual | Pro forma[a] |
| | (Dollars in millions) | | | |
| Revenues | $ 806 | $1,119 | $ 898 | $1,095 |
| Costs and expenses | (798) | (898) | (773) | (938) |
| Segment operating income | $ 8 | $ 221 | $ 125 | $ 157 |
| Segment ROI | 1.4% | 37.7% | 34.6% | 43.5% |

[a] Pro forma to reflect the results of operations from Standard Gypsum LP as if the acquisition occurred at the beginning of 2005.

Fluctuation in product pricing, which includes freight and is net of discounts, and shipments are set forth below:

| | Year over Year Increase (Decrease) | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| Lumber: | | | |
| Average prices | (13)% | (16)% | 5% |
| Shipments | 1% | 7% | 1% |
| Gypsum wallboard: | | | |
| Average prices | (27)% | 26% | 16% |
| Shipments | (26)% | 132% | 12% |
| Particleboard: | | | |
| Average prices | 2% | 15% | (1)% |
| Shipments | (17)% | (5)% | 8% |
| MDF: | | | |
| Average prices | 1% | 5% | (1)% |
| Shipments | (5)% | (30)% | (20)% |

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Demand for most products was down due to challenging market conditions in the housing industry. We expect this trend to continue in 2008.

Segment operating income also includes our share of income from our gypsum wallboard joint venture (in 2005) and MDF joint venture of $1 million in 2007, $3 million in 2006, and $28 million in 2005. The operating results from the joint ventures generally fluctuate in relation to the price and shipment changes noted above.

Costs and expenses were down 11 percent in 2007 compared with 2006, and up 16 percent in 2006 compared with 2005. The lower costs in 2007 were primarily driven by lower volumes. The increase in cost in 2006 is primarily attributable to the acquisition of Standard Gypsum LP in January 2006, partially offset by lower wood fiber costs and cost reductions attributable to the sale of our Pembroke MDF facility in June 2005.

Fluctuations in our significant cost and expense components included:

| | Year over Year Increase (Decrease) | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| | (In millions) | | |
| Wood fiber | $(32) | $(12) | $19 |
| Energy, principally natural gas | (21) | 16 | 13 |
| Freight | (12) | 26 | 11 |
| Chemicals | (5) | (1) | 14 |
| Depreciation | 1 | 9 | (3) |
| Health care | 1 | (1) | (6) |
| Pension and postretirement | 1 | (3) | 2 |

The cost of our fiber, energy, freight, and chemicals fluctuates based on the market prices we pay for these commodities. It is likely that these costs will continue to fluctuate in 2008.

Information about our converting and manufacturing facilities follows:

| | For the Year | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| Number of converting and manufacturing facilities (at year end) | 16 | 17 | 17 |
| Average operating rates for all product lines excluding sold or closed facilities: | | | |
| High | 102% | 106% | 102% |
| Low | 59% | 86% | 91% |
| Gypsum facing paper purchases from our Premier Boxboard Limited LLC joint venture, in thousand tons | 42 | 68 | 71 |
| Percent of gypsum facing paper supplied by our Premier Boxboard Limited LLC joint venture | 65% | 76% | 77% |

Markets for our building products continue to be challenging. Production in our converting operations is being reduced to match demand for our products. In December 2007, we permanently ceased production at our Mt. Jewett particleboard manufacturing plant.

**Timber and Timberland**

Timber and timberland, which managed our timber resources, is no longer an active segment as a result of the sale of timber and timberland in October 2007.

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A summary of our timber and timberland results follows:

| | For the Year | | |
|---|---|---|---|
| | 2007[a] | 2006 | 2005 |
| | (Dollars in millions) | | |
| Revenues | $ 76 | $ 89 | $ 120 |
| Costs and expenses | (11) | (26) | (48) |
| Segment operating income | $ 65 | $ 63 | $ 72 |
| Segment ROI | 20.4% | 19.5% | 18.0% |

[a] Reflects ten months of operating results.

In 2005, we sold about 7,000 acres of timber and timberland to a joint venture in which our former real estate segment owned a 50 percent interest and an unrelated public company owned the other 50 percent. This acreage was sold pursuant to the terms of a long-standing option agreement, which was about to expire. The joint venture intended to hold the land for future development and sale. We recognized about half of the $10 million gain in income in 2005 and recognized the remainder in 2007 when we spun-off our real estate segment. As a result of Hurricane Rita, we recorded a $7 million loss due to damage to our timberland in 2005, which is not included in segment operating income.

Information about our timber harvest follows:

| | For the Year | | |
|---|---|---|---|
| | 2007[a] | 2006 | 2005 |
| Timber harvest, in million tons: | | | |
| Sawtimber | 2.1 | 2.6 | 2.4 |
| Pulpwood | 2.9 | 3.4 | 3.3 |
| | 5.0 | 6.0 | 5.7 |

[a] Reflects ten months of operating results.

**Income and Expenses Not Allocated to Segments**

Unallocated income and expenses represent expenses managed on a company-wide basis and include corporate general and administrative expense, share-based compensation, other operating and non-operating income (expense), and interest income and expense.

The decrease in general and administrative expense in 2007 was principally due to a decrease in incentive compensation. Incentive compensation fluctuates based on changes in ROI.

Our share-based compensation fluctuates because a significant portion of our share-based awards are cash based and are affected by changes in the market price of our common stock. Based on our current expectations, it is likely that share-based compensation expense for 2008 will be in the range of $20 million to $30 million.

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Other operating income (expense) not allocated to business segments consists of:

| | For the Year | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| | (In millions) | | |
| Transformation costs | $ (69) | $— | $ — |
| Closure and sale of converting and production facilities and sale of non-strategic assets | (55) | (4) | (50) |
| Litigation | (56) | (6) | (13) |
| Environmental remediation | (9) | (8) | (3) |
| Softwood Lumber Agreement | — | 42 | — |
| Hurricane related costs and, in 2006, related insurance proceeds | — | 2 | (16) |
| Other | 1 | — | (3) |
| | $(188) | $26 | $(85) |

We continue our efforts to enhance return on investment by lowering costs, improving operating efficiencies, and increasing asset utilization. As a result, we continue to review operations that are unable to meet return objectives and determine appropriate courses of action, including possibly consolidating and closing facilities and selling under-performing assets. In 2007, we permanently ceased production at our particleboard plant in Mt. Jewett, Pennsylvania and recognized a $64 million charge, primarily related to the present value of remaining lease payments under our long-term operating lease of the plant and impairment of the related equipment.

Also, in December 2007, we resolved most of the remaining claims regarding an alleged violation of Section 1 of the Sherman Act and recognized a charge of $46 million. We are also defending two cases in California state court alleging violations of that state's on-duty meal break laws. In 2007, we settled three additional meal break cases.

In 2006, the U.S. and Canada entered into the Softwood Lumber Agreement, which provided for the refund to domestic lumber producers of a portion of duties previously collected by the U.S. government. Our portion of this refund was $42 million.

Other non-operating income (expense) includes $40 million of expenses associated with the early repayment of debt in 2007 and a gain of $89 million related to the settlement of tax litigation in 2006.

Net interest income on financial assets and nonrecourse financial liabilities of special purpose entities relates to interest income on the $2.38 billion of notes received from the sale of our timberland in October 2007 and interest expense on the $2.14 billion of borrowings secured by a pledge of the notes receivable in December 2007. The notes receivable were contributed to and the borrowings were made by two wholly-owned, bankruptcy-remote special purpose entities, which we consolidate for financial reporting purposes. The borrowings are nonrecourse to us.

The change in interest expense in 2007 was due to lower average levels of debt outstanding compared with 2006. At year-end 2007, we had $0.9 billion of debt with fixed interest rates that averaged 7.08 percent. This compares with $1.4 billion of debt with fixed interest rates that averaged 7.02 percent and $0.2 billion of debt with variable interest rates that averaged 5.88 percent at year-end 2006.

**Income Taxes**

Our effective tax rate, which is income tax expense (benefit) as a percentage of income from continuing operations before taxes, was 39 percent in 2007, 26 percent in 2006, and (64) percent in 2005. These rates reflect in 2007, non-deductible transformation related expenses, one-time tax benefit of $3 million related to changes to the State of Texas margin tax and a $4 million benefit from the resolution of state tax matters; in 2006, one-time benefits resulting from settlement of tax litigation with the U.S. Government and the new State of Texas margin tax; and in 2005, a one-time benefit related to the sale of a foreign subsidiary.

We anticipate that our effective tax rate in 2008 will approximate 40 percent.

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### Discontinued Operations

On December 28, 2007, we spun off to our shareholders in tax free distributions, our real estate segment and financial services segment, which included certain real estate and minerals activities in our timber and timberland segment.

As a result, we report the results of operations of these segments as discontinued operations. Expenses allocated to these discontinued operations included interest expense of $7 million in 2007, $4 million in 2006, and none in 2005 and share-based compensation expense of $7 million in 2007, $8 million in 2006, and $5 million in 2005.

In addition, on August 31, 2007 we sold our previously acquired chemical operations. We received cash proceeds of $1 million and recognized a pre-tax loss of $6 million on the sale.

A summary of earnings from our discontinued operations follows:

| | For the Year | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| | (In millions) | | |
| Real estate income before taxes | $ 41 | $ 83 | $ 59 |
| Financial services income before taxes | 138 | 204 | 192 |
| Chemical operations and other[a] | (13) | (2) | 1 |
| Income from discontinued operations before taxes | 166 | 285 | 252 |
| Income tax expense | (63) | (104) | (94) |
| Discontinued operations | $103 | $ 181 | $158 |

[a] 2007 includes a $6 million charge for environmental remediation.

### Average Shares Outstanding

Average shares outstanding and average diluted shares outstanding decreased in 2007, 2006, and 2005 due to the effects of share repurchases in 2006 and 2005.

### Capital Resources and Liquidity

### Sources and Uses of Cash

Cash from operations was $296 million in 2007, $780 million in 2006, and $508 million in 2005.

We operate in cyclical industries and our operating cash flows vary accordingly. Our principal operating cash requirements are for compensation, wood and recycled fiber, energy, interest, and taxes. We experienced improved pricing and shipments for most of our products in 2006 and 2005, but experienced deterioration in pricing and volume for our building products in 2007 due to challenging conditions in the housing market. Working capital is subject to cyclical operating needs, the timing of collection of receivables and the payment of payables and expenses and, to a lesser extent, to seasonal fluctuations in our operations.

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| | For the Year | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| | (In millions) | | |
| We received cash from: | | | |
| Operations | $ 296 | $ 649 | $ 508 |
| Tax litigation settlement, net | — | 89 | — |
| Softwood Lumber Agreement payments | — | 42 | — |
| From operations | 296 | 780 | 508 |
| Exercise of options and in 2005 the settlement of equity purchase contracts | 35 | 57 | 393 |
| Nonrecourse borrowing secured by financial assets of special purpose entities (net of costs of $4 million) | 2,136 | — | — |
| Borrowings, net | — | 40 | 13 |
| Other | 36 | 64 | 45 |
| Total sources | 2,503 | 941 | 959 |
| We used cash to: | | | |
| Reduce borrowings, net (including $38 million of debt tender premium) | (780) | — | — |
| Return to shareholders through: | | | |
| Dividends | (1,212) | (108) | (102) |
| Repurchase of common stock | (24) | (318) | (527) |
| Reinvest in the business through: | | | |
| Capital expenditures | (237) | (204) | (220) |
| Acquisition, joint ventures, and other | (21) | (149) | (23) |
| Total uses | (2,274) | (779) | (872) |
| Discontinued operations, net | (32) | (132) | (96) |
| Change in cash and cash equivalents | $ 197 | $ 30 | $ (9) |

We issued 1,009,246 net shares of common stock in 2007; 1,736,335 net shares of common stock in 2006; and 1,833,688 net shares in 2005 to employees exercising options. In addition, in 2005, we issued 10,875,739 shares of our common stock and received $345 million in cash in conjunction with the final settlement of our Upper DECS(SM) equity purchase contracts.

We paid cash dividends to shareholders of $11.37 per share in 2007 including a special dividend of $10.25 per share, $1.00 per share in 2006, and $0.90 per share in 2005. On February 1, 2008, our Board of Directors declared a regular quarterly dividend of $0.10 per share payable on March 14, 2008.

From February 2005 through year-end 2007, our Board of Directors approved repurchase programs aggregating 29.0 million shares. As of year-end 2007, we had repurchased 22.4 million shares under these programs. In 2007, we initiated no share purchases, but we settled $24 million of share purchases that were initiated in fourth quarter 2006. As of year-end 2007, there are 6.6 million shares remaining under current repurchase authorizations.

Capital expenditures and timberland reforestation were 111 percent of depreciation and amortization in 2007, 91 percent in 2006, and 101 percent in 2005. Most of the 2007 expenditures relate to initiatives to increase reliability and efficiency at our linerboard mills and increase asset utilization in our converting facilities. Capital expenditures are expected to approximate $195 million in 2008, or about 97 percent of expected 2008 depreciation and amortization.

In 2007, we reduced our outstanding debt by $742 million, principally with proceeds from the transactions related to our transformation plan. In 2006, we used $150 million of our credit facilities to fund

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the purchase of the remaining 50 percent interest in Standard Gypsum LP. Following the purchase, we paid off $56 million of the venture's long-term debt, of which $28 million was related to the purchased interest. In 2005, market conditions provided the opportunity to lengthen our debt maturity profile in a cost effective manner. As a result, we issued $250 million of debt due in 2016 and $250 million of debt due in 2018. The proceeds were used to refinance debt due in 2006 and 2007.

**Liquidity and Contractual Obligations**

At year-end 2007 our contractual obligations consist of:

| | Payments Due or Expiring by Year | | | | |
|---|---|---|---|---|---|
| | Total | 2008 | 2009-10 | 2011-12 | Thereafter |
| | | | (In millions) | | |
| Long-term debt (including current maturities)[a] | $ 855 | $ 13 | $ 35 | $294 | $ 513 |
| Nonrecourse financial liabilities of special purposes entities[a] | 2,140 | — | — | — | 2,140 |
| Less, related financial assets of special purpose entities[a] | (2,140) | — | — | — | (2,140) |
| Principal portion of capital lease obligations[a] | 188 | — | — | — | 188 |
| Less, related municipal bonds we own[a] | (188) | — | — | — | (188) |
| Contractual interest payments on fixed- rate, long-term debt and capital lease obligations, net of interest on related municipal bonds we own | 437 | 60 | 117 | 116 | 144 |
| Operating leases[b] | 222 | 38 | 61 | 40 | 83 |
| Purchase obligations[c] | 3,173 | 265 | 445 | 441 | 2,022 |
| Other long-term liabilities[a] | 37 | 7 | 21 | 2 | 7 |
| | $ 4,724 | $383 | $679 | $893 | $ 2,769 |

[a] Denotes items included on our balance sheet.

[b] In 2007, we recorded an impairment charge related to a long-term operating lease. As a result, $60 million present value of our future operating lease payments are included on our balance sheet, of which, $3 million is in current liabilities and $57 million in other long-term liabilities.

[c] In 2007, we entered into a 20-year fiber supply agreement for pulpwood and a 12-year fiber supply agreement for sawtimber, the terms of which are both subject to extension. These purchase obligations are valued at year-end 2007 market prices, however, our actual future purchases will be at the then current market price.

Our sources of short-term funding are our operating cash flows and borrowings under our credit agreements and accounts receivable securitization facility. Our contractual obligations due in 2008 will likely be repaid from our operating cash flow or from our unused borrowing capacity. At year-end 2007, we had $1.067 billion in unused borrowing capacity under our committed credit agreements and accounts receivable securitization facility:

| | Committed Credit Agreements | Accounts Receivable Securitization Facility | Total |
|---|---|---|---|
| | | (In millions) | |
| Committed | $835 | $247 | $1,082 |
| Less: borrowings and commitments | (14) | (1) | (15) |
| Unused borrowing capacity at year-end 2007 | $821 | $246 | $1,067 |

Our committed credit agreements include a $750 million revolving credit facility that expires in 2011. The remainder of the committed agreements expire between 2008 and 2010.

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Our accounts receivable securitization facility expires in 2010. Under this facility, a wholly-owned, bankruptcy-remote subsidiary purchases, on an on-going basis, substantially all of our trade receivables. As we need funds, the subsidiary draws under its revolving credit agreement, pledges the trade receivables as collateral, and remits the proceeds to us. In the event of liquidation of the subsidiary, its creditors would be entitled to satisfy their claims from the subsidiary's pledged receivables prior to distributions back to us. We included this subsidiary in our consolidated financial statements.

Our debt agreements, accounts receivable securitization facility, and credit agreements contain terms, conditions, and financial covenants customary for such agreements including minimum levels of interest coverage and limitations on leverage. At year-end 2007, we had complied with the terms, conditions, and financial covenants of these agreements. None of our credit agreements or the accounts receivable securitization facility are restricted as to availability based on the ratings of our long-term debt. Under the terms of our Senior Notes due 2016 and Senior Notes due 2018, the interest rate on the notes automatically adjusts if our long-term debt rating is decreased below investment grade by Moody's Investor Services, Inc. (Moody's) or Standard and Poor's Rating Services, a division of McGraw-Hill, Inc. (S&P). The interest rate on these notes was increased 25 basis points during third quarter 2007 following a change in our long-term debt rating by Moody's. In addition, as required by our operating lease agreements for our particleboard and MDF facilities in Mt. Jewett, Pennsylvania, we provided an $11 million letter of credit to support a portion of our obligations due to this change in our long-term debt rating. Our long-term debt is currently rated BBB- by S&P and Ba1 by Moody's. At year-end 2007, property and equipment having a book value of $2 million were subject to liens in connection with $14 million of debt.

Operating leases represent pre-tax obligations and include $146 million for the lease of particleboard and MDF facilities in Mt. Jewett, Pennsylvania, which expire in 2019. The rest of our operating lease obligations are for facilities and equipment. As a result of an impairment charge in 2007, $60 million present value of our operating lease obligations is included on our balance sheet, of which $3 million is in current liabilities and $57 million is in other long-term liabilities.

In 2007, we received $2.38 billion in notes from the sale of timberland, which we contributed to two wholly-owned, bankruptcy-remote special purpose entities. The notes are secured by irrevocable letters of credit and are due in 2027. The special purpose entities pledged the notes and irrevocable letters of credit to secure $2.14 billion nonrecourse loans payable in 2027. In the event of liquidation of the special purpose entities, these creditors would be entitled to satisfy their claims from the pledged notes and irrevocable letters of credit prior to distributions back to us. We include these special purpose entities in our consolidated financial statements.

In the 1990's, we entered into two sale-lease back transactions of production facilities with municipalities. We entered into these transactions to mitigate property and similar taxes associated with these facilities. The municipalities purchased these facilities from us for $188 million, our carrying value, and we leased the facilities back from the municipalities under lease agreements, which expire in 2022 and 2025. Concurrently, we purchased $188 million of interest-bearing bonds issued by these municipalities. The bond terms are identical to the lease terms, are secured by payments under the capital lease obligations, and the municipalities are obligated only to the extent the underlying lease payments are made by us. The interest rate implicit in the leases is the same as the interest rate on the bonds. As a result, the present value of the capital lease obligations is $188 million, the same as the principal amount of the bonds. Since there is no legal right of offset, the $188 million of bonds are included in other assets and the $188 million present value of the capital lease obligations are included in other long-term liabilities. There is no net effect from these transactions as we are in substance both the obligor on, and the holder of, the bonds.

Purchase obligations are market priced obligations principally for pulpwood, timber, and gypsum used in our manufacturing and converting processes and for major committed capital expenditures.

We have other long-term liabilities, principally liabilities for pension and postretirement benefits, unrecognized tax benefits, and deferred income taxes that are not included in the table because they do not have scheduled maturities.

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At year-end 2007, the liability for pension benefits was $119 million and the liability for postretirement benefits was $137 million. We expect our 2008 voluntary, discretionary contributions to our defined benefit pension plan to approximate 2008 service cost, which is estimated to be about $30 million. In addition, we have amended our supplemental defined benefit pension plan to allow for lump-sum settlements at the time of retirement. We offered a one-time window for our current retirees to take a lump-sum distribution in January 2008. We expect these lump-sum payments to aggregate $42 million in 2008. We also estimate that we will be required to pay in the range of $17 million to $20 million per year over the next five years to fund payments to participants of our supplemental defined benefit plan and retiree health care claims. Please read **Pension, Postretirement Medical and Health Care Matters** for additional information.

At year-end 2007, our net deferred income tax liability was $663 million, including $286 million of alternative minimum tax credits related to the 2007 sale of our timberland. We do not expect any significant changes in our deferred tax liability in 2008. We expect our cash tax rate in 2008 to be below 20 percent compared with 15 percent in 2007. The cash tax rate is impacted by utilization of our alternative minimum tax credits and deductions for 2008 payments associated with our 2007 transformation.

We have interest rate derivative instruments outstanding at year-end 2007. These interest rate instruments expire in 2008. They are non-exchange traded and are valued using either third-party resources or models. At year-end 2007, the aggregate fair value of our interest rate instruments was a $1 million liability.

**Off-Balance Sheet Arrangements**

From time to time, we enter into off-balance sheet arrangements to facilitate our operating activities. At year-end 2007, our off-balance sheet unfunded arrangements, excluding contractual interest payments, operating leases, and purchase and other obligations included in the table of contractual obligations, consisted of:

| | Expiring by Year | | | | |
|---|---|---|---|---|---|
| | Total | 2008 | 2009-10 | 2011-12 | Thereafter |
| | (In millions) | | | | |
| Joint venture guarantees | $ 70 | $18 | $52 | $— | $— |
| Performance bonds and recourse obligations | 56 | 56 | — | — | — |
| | $126 | $74 | $52 | $— | $— |

We participate in two joint ventures engaged in manufacturing and selling paper and building products. Our partner in each of these ventures is a publicly-held company unrelated to us. At year-end 2007, these ventures had $85 million in long-term debt and $6 million of debt included in current maturities, along with various letters of credit. We guaranteed $70 million of the joint ventures' debt service obligations and letters of credit. Our joint venture partners also provided guarantees and letters of credit. Generally we would be called upon to fund the guarantees due to the lack of specific performance by the joint ventures, such as non-payment of debt.

Performance bonds and recourse obligations are primarily for workers' compensation and general liability claims.

**Pension, Postretirement Medical and Health Care Matters**

Our non-cash defined benefit pension expense was $35 million in 2007, $46 million in 2006, and $49 million in 2005. For the year 2008, we expect our non-cash defined benefit pension expense to be about $37 million. We also expect a one-time expense of $15 million related to lump sum settlements of supplemental benefits.

For accounting purposes, we measure the projected benefit obligation of our defined benefit plans and value the plan assets as of year-end 2007 to determine the funded status. The funded status is included on our balance sheet. At year-end 2007, the funded status of our defined benefit plans was a liability of $119 million compared with a liability of $231 million at year-end 2006. The change was principally due to an increase in the discount rate, a better than expected return on plan assets, and an increase in plan assets due in part to the $60 million of voluntary, discretionary contributions we made in 2007. Unrecognized actuarial losses, which

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are included in accumulated other comprehensive income and principally represent the delayed recognition of changes in the assumed discount rate and differences between expected and actual returns, were $166 million at year-end 2007 and $253 million at year-end 2006. These losses will be recognized over the average remaining service period of our current employees, which is about nine years. We expect about $5 million of these losses will be recognized in 2008, compared with $14 million recognized in 2007.

We did not have any ERISA cash-funding requirement in 2007, and we expect our cash-funding requirement to be minimal in 2008. We made voluntary, discretionary contributions of $60 million to the defined benefit plan in 2007. We expect our 2008 voluntary, discretionary contributions to our defined benefit plan to approximate 2008 service cost, which is estimated to be about $30 million. Passage of the Pension Protection Act of 2006, which requires a minimum level of annual funding, is not expected to affect significantly our annual cash contributions.

The benefits payable from our defined benefit plan are a series of fixed monthly retirement payments. On an annual basis an actuarial assessment of the estimated amount and timing of these retirement payments is performed. The actuarial estimate is subject to variability due to changes in key assumptions regarding future wage inflation, participant mortality and other actuarial risks. Prior to the date of retirement, our obligation is to accumulate funds in our qualified plan sufficient to meet these related benefit payments. The weighted average timeframe of the retirement payments is generally in the 10-15 year range.

The benefit obligation, which is the present value of the estimated retirement payments, conceptually is very similar to the fair value of a portfolio of long-term bonds. The funded status of our benefit obligation that is matched by long-term bonds of similar duration should remain relatively unchanged even if long-term interest rates change.

In the last two months of 2007, we transitioned to a more matched position between our assets and liabilities in our qualified defined benefit plan. This action is expected to reduce the volatility of our defined benefit expense and our funding requirements. As a result, our expected long-term rate of return for 2008 expense is 6.875 percent compared with the 2007 rate of 8 percent. The lower expected long-term rate of return reflects the higher allocation of invested funds in fixed income securities that better match our defined benefit obligation.

For accounting purposes we measure the postretirement medical plans projected benefit obligation as of year-end 2007 to determine the funded status. At year-end 2007, the funded status of these plans was a liability of $137 million compared with $135 million at year-end 2006.

About 26 percent of our employees participated in a consumer driven health plan in 2007 compared with 29 percent in 2006. In 2007, the total cost of providing health benefits was about $88 million of which we incurred $57 million and our employees incurred $31 million. In 2006, the total cost of providing health benefits was about $97 million of which we incurred $67 million and our employees incurred $30 million.

**Energy and the Effects of Inflation**

Energy costs decreased $22 million in 2007, increased $8 million in 2006, and increased $43 million in 2005. The decrease in 2007 is primarily attributable to reduced production because of the decreased demand for our building products as a result of the declines in the housing industry. The increase in energy costs for 2006 is primarily attributable to the acquisition of Standard Gypsum LP in January 2006. Our energy costs fluctuate based on the market prices we pay. We hedge very little of our energy needs. It is likely that these costs will continue to fluctuate in 2008.

Inflationary increases in compensation and certain input costs such as fiber, energy and freight have had a negative impact on our operating results. However, we have managed to partially offset the impact of inflation through increased productivity. Our fixed assets are, and our timber and timberland were, carried at historical costs. If carried at current replacement costs, depreciation expense and the cost of timber cut or timberland sold would have been significantly higher than what we reported.

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### Environmental Protection

Our operations are subject to federal, state, and local provisions regulating discharges into the environment and otherwise related to the protection of the environment. Compliance with these provisions requires us to invest substantial funds to modify facilities to assure compliance with applicable environmental regulations. A more detailed discussion regarding our compliance with environmental regulation can be found in **Business — Environmental Regulation**.

### Litigation Matters

We are involved in various legal proceedings that arise from time to time in the ordinary course of doing business. In our opinion, the possibility of a material loss from any of these proceedings is considered to be remote, and we do not expect that the effect of these proceedings will be material to our financial position, results of operations, or cash flow. It is possible, however, that charges related to these matters could be significant to results of operations or cash flows in any one accounting period. A more detailed discussion regarding our most significant litigation matters can be found in **Legal Proceedings**.

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## Calculation of Non-GAAP Financial Measures

| | Consolidated | Corrugated Packaging | Building Products | Timber and Timberland |
|---|---|---|---|---|
| | | (Dollars in millions) | | |
| **Year 2007** | | | | |
| Return: | | | | |
| Segment operating income determined in accordance with GAAP | $ 360 | $ 287 | $ 8 | $ 65 |
| Expenses not allocated to segments: | | | | |
| General and administrative | (100) | N/A | N/A | N/A |
| Share-based compensation | (34) | N/A | N/A | N/A |
| | $ 226 | $ 287 | $ 8 | $ 65 |
| Investment: | | | | |
| Beginning of year total assets or segment assets determined in accordance with GAAP | $ 20,474 | $2,275 | $ 638 | $ 330 |
| Adjustments: | | | | |
| Current liabilities (excluding current portion of long-term debt) | (550) | (271) | (76) | (11) |
| Assets of discontinued operations | (16,847) | N/A | N/A | N/A |
| Municipal bonds related to capital leases included in other assets | (188) | N/A | N/A | N/A |
| | $ 2,889 | $2,004 | $ 562 | $ 319 |
| ROI | 7.8% | 14.3% | 1.4% | 20.4% |
| **Year 2006** | | | | |
| Return: | | | | |
| Segment operating income determined in accordance with GAAP | $ 539 | $ 255 | $ 221 | $ 63 |
| Expenses not allocated to segments: | | | | |
| General and administrative | (107) | N/A | N/A | N/A |
| Share-based compensation | (38) | N/A | N/A | N/A |
| | $ 394 | $ 255 | $ 221 | $ 63 |
| Investment: | | | | |
| Beginning of year total assets or segment assets determined in accordance with GAAP | $ 21,630 | $2,308 | $ 456 | $ 333 |
| Adjustments: | | | | |
| Current liabilities (excluding current portion of long-term debt) | (476) | (269) | (66) | (10) |
| Assets of discontinued operations | (18,219) | N/A | N/A | N/A |
| Municipal bonds related to capital leases included in other assets | (188) | N/A | N/A | N/A |
| Acquisition of Standard Gypsum LP in January 2006 | 196 | N/A | 196 | N/A |
| | $ 2,943 | $2,039 | $ 586 | $ 323 |
| ROI | 13.4% | 12.5% | 37.7% | 19.5% |
| **Year 2005** | | | | |
| Return: | | | | |
| Segment operating income determined in accordance with GAAP | $ 317 | $ 120 | $ 125 | $ 72 |
| Expenses not allocated to segments: | | | | |
| General and administrative | (91) | N/A | N/A | N/A |
| Share-based compensation | (21) | N/A | N/A | N/A |
| | $ 205 | $ 120 | $ 125 | $ 72 |
| Investment: | | | | |
| Beginning of year total assets or segment assets determined in accordance with GAAP | $ 20,144 | $2,448 | $ 423 | $ 409 |
| Adjustments: | | | | |
| Current liabilities (excluding current portion of long-term debt) | (503) | (323) | (62) | (9) |
| Assets of discontinued operations | (16,622) | N/A | N/A | N/A |
| Municipal bonds related to capital leases included in other assets | (188) | N/A | N/A | N/A |
| | $ 2,831 | $2,125 | $ 361 | $ 400 |
| ROI | 7.2% | 5.6% | 34.6% | 18.0% |

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## Statistical and Other Data

Revenues and unit sales, excluding joint venture operations, follows:

| | For the Year | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| | (Dollars in millions) | | |
| ***Revenues*** | | | |
| **Corrugated Packaging** | | | |
| Corrugated packaging | $2,905 | $2,841 | $2,728 |
| Linerboard | 139 | 136 | 97 |
| | $3,044 | $2,977 | $2,825 |
| **Building Products** | | | |
| Pine lumber | $ 244 | $ 278 | $ 312 |
| Particleboard | 181 | 214 | 195 |
| Gypsum wallboard[(a)] | 228 | 420 | 143 |
| Medium density fiberboard[(a)] | 62 | 65 | 87 |
| Fiberboard | 52 | 72 | 83 |
| Other | 39 | 70 | 78 |
| | $ 806 | $1,119 | $ 898 |
| **Timber and Timberland** | | | |
| Fiber and other | $ 76 | $ 89 | $ 120 |
| ***Unit sales*** | | | |
| **Corrugated Packaging** | | | |
| Corrugated packaging, thousands of tons | 3,351 | 3,371 | 3,437 |
| Linerboard, thousands of tons | 303 | 310 | 264 |
| | 3,654 | 3,681 | 3,701 |
| **Building Products** | | | |
| Pine lumber, million board feet | 838 | 829 | 777 |
| Particleboard, million square feet | 506 | 609 | 640 |
| Gypsum wallboard, million square feet[(a)] | 1,475 | 1,990 | 859 |
| Medium density fiberboard, million square feet[(a)] | 135 | 142 | 202 |
| Fiberboard, million square feet | 288 | 362 | 431 |

[(a)] Comparisons of revenue and unit sales of gypsum wallboard are affected by the 2006 acquisition of our partner's interest in Standard Gypsum LP. Comparisons for MDF are affected by the sale of the Pembroke facility in second quarter 2005.

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## Item 7A. *Quantitative and Qualitative Disclosures About Market Risk*

### Interest Rate Risk

Our current level of interest rate risk is primarily due to our variable-rate, long-term debt and financial assets and nonrecourse financial liabilities of special purpose entities. The following table illustrates the estimated effect on our pre-tax income of immediate, parallel, and sustained shifts in interest rates for the next 12 months at year-end 2007, with comparative year-end 2006 information. These estimates assume that debt reductions from contractual payments will be replaced with short-term, variable-rate debt; however, that may not be the financing alternative we choose to follow.

| Change in Interest Rates | Increase (Decrease) in Income Before Taxes | |
|---|---|---|
| | At Year-End 2007 | At Year-End 2006 |
| | (In millions) | |
| +2% | $(4) | $(3) |
| +1% | (2) | (2) |
| −1% | 2 | 2 |
| −2% | 4 | 4 |

Interest rate changes impact earnings due to the resulting increase or decrease in the cost of our variable-rate, long-term debt. The interest rate sensitivity change from year-end 2006 is due to a decrease in variable-rate debt. Additionally, changes in interest rates will affect the value of our interest rate swap agreements (currently $50 million notional amount). We believe that any changes in the value of these agreements would not be significant.

### Foreign Currency Risk

We do not have significant exposure to foreign currency fluctuations on our financial instruments because most of these instruments are denominated in U.S. dollars.

### Commodity Price Risk

From time to time we use commodity derivative instruments to mitigate our exposure to changes in product pricing and manufacturing costs. These instruments cover a small portion of our volume and range in duration from three months to three years. Considering the fair value of these instruments at year-end 2007, we believe the potential loss in fair value resulting from a hypothetical ten percent change in the underlying commodity prices would not be significant.

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**Item 8.** ***Financial Statements and Supplementary Data***


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## MANAGEMENT'S ANNUAL REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

The management of Temple-Inland is responsible for establishing and maintaining adequate internal control over financial reporting. Management has designed our internal control over financial reporting to provide reasonable assurance that our published financial statements are fairly presented, in all material respects, in conformity with generally accepted accounting principles.

Management is required by paragraph (c) of Rule 13a-15 of the Securities Exchange Act of 1934, as amended, to assess the effectiveness of our internal control over financial reporting as of each year end. In making this assessment, management used the *Internal Control — Integrated Framework* issued in July 1994 by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

Management conducted the required assessment of the effectiveness of our internal control over financial reporting as of year end. Based upon this assessment, management believes that our internal control over financial reporting is effective as of year-end 2007.

Ernst & Young LLP, the independent registered public accounting firm that audited our financial statements included in this Form 10-K, has also audited our internal control over financial reporting. Their attestation report follows this report of management.

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## REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

**The Board of Directors and Shareholders of Temple-Inland Inc.:**

We have audited Temple-Inland Inc's internal control over financial reporting as of December 29, 2007 based on criteria established in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria). Temple-Inland Inc.'s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting including in the accompanying Management's Annual Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on the effectiveness of the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, Temple-Inland Inc. and subsidiaries maintained, in all material respects, effective internal control over financial reporting as of December 29, 2007 based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Temple-Inland Inc. and subsidiaries as of December 29, 2007 and December 30, 2006 and the related consolidated statements of income, shareholders' equity, and cash flows for each of the three years in the period ended December 29, 2007 and our report dated February 25, 2008 expressed an unqualified opinion thereon.

Ernst & Young LLP

Austin, Texas
February 25, 2008

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## REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

**The Board of Directors and Shareholders of Temple-Inland Inc.:**

We have audited the accompanying consolidated balance sheets of Temple-Inland Inc. and subsidiaries as of December 29, 2007 and December 30, 2006, and the related consolidated statements of income, shareholders' equity, and cash flows for each of the three years in the period ended December 29, 2007. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Temple-Inland Inc. and subsidiaries at December 29, 2007 and December 30, 2006, and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 29, 2007, in conformity with U.S. generally accepted accounting principles.

As discussed in Note 1 to the Consolidated Financial Statements, in 2006, the Company changed its method of accounting for the funded status of defined pension and other postretirement benefit plans, and in 2007 the Company changed the measurement date for measuring the funded status of defined pension and other postretirement benefit plans. Additionally, during 2007 the Company changed its method of accounting for and disclosure of uncertainties associated with certain aspects of measurement and recognition of income taxes.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of Temple-Inland Inc.'s internal control over financial reporting as of December 29, 2007, based on criteria established in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated February 25, 2008 expressed an unqualified opinion thereon.

Ernst & Young LLP

Austin, Texas
February 25, 2008

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## TEMPLE-INLAND INC. AND SUBSIDIARIES

## CONSOLIDATED BALANCE SHEETS

| | At Year-End | |
|---|---|---|
| | 2007 | 2006 |
| | (In millions) | |
| **ASSETS** | | |
| **Current Assets** | | |
| Cash and cash equivalents | $ 227 | $ 30 |
| Trade receivables, net of allowance for doubtful accounts of $14 in 2007 and $14 in 2006 | 433 | 452 |
| Inventories: | | |
| Work in process and finished goods | 116 | 109 |
| Raw materials | 224 | 211 |
| Supplies and other | 121 | 115 |
| Total inventories | 461 | 435 |
| Deferred tax asset | 99 | 61 |
| Prepaid expenses and other | 57 | 60 |
| Total current assets | 1,277 | 1,038 |
| **Timber and Timberland** | — | 315 |
| **Property and Equipment** | | |
| Land and buildings | 641 | 637 |
| Machinery and equipment | 3,423 | 3,400 |
| Construction in progress | 120 | 82 |
| Less allowances for depreciation | (2,552) | (2,491) |
| Total property and equipment | 1,632 | 1,628 |
| **Financial Assets of Special Purpose Entities** | 2,383 | — |
| **Goodwill** | 365 | 365 |
| **Assets of Discontinued Operations** | — | 16,847 |
| **Other Assets** | 285 | 281 |
| **TOTAL ASSETS** | $ 5,942 | $20,474 |
| **LIABILITIES** | | |
| **Current Liabilities** | | |
| Accounts payable | $ 244 | $ 229 |
| Accrued employee compensation and benefits | 108 | 126 |
| Accrued interest | 31 | 32 |
| Accrued property taxes | 11 | 19 |
| Accrued income taxes | 258 | — |
| Other accrued expenses | 173 | 129 |
| Current portion of long-term debt | 3 | 13 |
| Current portion of pension and postretirement benefits | 62 | 15 |
| Total current liabilities | 890 | 563 |
| **Long-Term Debt** | 852 | 1,584 |
| **Nonrecourse Financial Liabilities of Special Purpose Entities** | 2,140 | — |
| **Deferred Tax Liability** | 762 | 244 |
| **Liability for Pension Benefits** | 71 | 229 |
| **Liability for Postretirement Benefits** | 123 | 122 |
| **Liabilities of Discontinued Operations** | — | 15,291 |
| **Other Long-Term Liabilities** | 324 | 252 |
| **TOTAL LIABILITIES** | 5,162 | 18,285 |
| **SHAREHOLDERS' EQUITY** | | |
| Preferred stock — par value $1 per share: authorized 25,000,000 shares; none issued | — | — |
| Common stock — par value $1 per share: authorized 200,000,000 shares; issued 123,605,344 shares in 2007 and 2006, including shares held in the treasury | 124 | 124 |
| Additional paid-in capital | 475 | 468 |
| Accumulated other comprehensive loss | (139) | (191) |
| Retained earnings | 987 | 2,501 |
| Cost of shares held in the treasury: 17,464,189 shares in 2007 and 18,754,907 shares in 2006 | (667) | (713) |
| **TOTAL SHAREHOLDERS' EQUITY** | 780 | 2,189 |
| **TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY** | $ 5,942 | $20,474 |

Please read the notes to consolidated financial statements.

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## TEMPLE-INLAND INC. AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF INCOME

| | For the Year | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| | | (In millions) | |
| **NET REVENUES** | $ 3,926 | $ 4,185 | $ 3,843 |
| **COSTS AND EXPENSES** | | | |
| Cost of sales | (3,390) | (3,476) | (3,382) |
| Selling | (112) | (107) | (97) |
| General and administrative | (197) | (214) | (198) |
| Gain on sale of timberland | 2,053 | — | — |
| Other operating income (expense) | (189) | 32 | (46) |
| | (1,835) | (3,765) | (3,723) |
| **OPERATING INCOME** | 2,091 | 420 | 120 |
| Other non-operating income (expense) | (35) | 93 | — |
| Interest income on financial assets of special purpose entities | 19 | — | — |
| Interest expense on nonrecourse financial liabilities of special purpose entities | (9) | — | — |
| Interest expense on debt | (111) | (123) | (109) |
| **INCOME FROM CONTINUING OPERATIONS BEFORE TAXES** | 1,955 | 390 | 11 |
| Income tax expense | (753) | (103) | 7 |
| **INCOME FROM CONTINUING OPERATIONS** | 1,202 | 287 | 18 |
| Discontinued operations | 103 | 181 | 158 |
| **NET INCOME** | $ 1,305 | $ 468 | $ 176 |
| **WEIGHTED AVERAGE COMMON SHARES OUTSTANDING** | | | |
| Basic | 106.0 | 108.8 | 112.6 |
| Diluted | 108.1 | 110.8 | 114.5 |
| **EARNINGS PER SHARE** | | | |
| **Basic:** | | | |
| Income from continuing operations | $ 11.33 | $ 2.64 | $ 0.16 |
| Discontinued operations | 0.98 | 1.66 | 1.40 |
| Net income | $ 12.31 | $ 4.30 | $ 1.56 |
| **Diluted:** | | | |
| Income from continuing operations | $ 11.12 | $ 2.59 | $ 0.16 |
| Discontinued operations | 0.96 | 1.63 | 1.38 |
| Net income | $ 12.08 | $ 4.22 | $ 1.54 |

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## TEMPLE-INLAND INC. AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF CASH FLOWS

| | For the Year | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| | (In millions) | | |
| **CASH PROVIDED BY (USED FOR) OPERATIONS** | | | |
| Net income | $ 1,305 | $ 468 | $ 176 |
| Adjustments: | | | |
| Gain on sale of timberland | (2,053) | — | — |
| Impairments | 64 | — | 24 |
| Loss on early payment of debt | 40 | — | — |
| Loss on sale of Pembroke | — | — | 25 |
| Depreciation and amortization | 214 | 225 | 218 |
| Non-cash share-based compensation | 39 | 38 | 26 |
| Non-cash pension and postretirement expense | 44 | 56 | 58 |
| Cash contribution to pension and postretirement plans | (80) | (76) | (76) |
| Deferred income taxes | 435 | 34 | 40 |
| Earnings of joint ventures | (5) | (11) | (39) |
| Dividends from joint ventures | 8 | 12 | 43 |
| Tax benefit of stock options exercised | — | — | 7 |
| Other | 14 | 18 | 16 |
| Changes in: | | | |
| Receivables | 19 | (28) | (16) |
| Inventories | (30) | (10) | — |
| Accounts payable and accrued expenses | 274 | 32 | 4 |
| Prepaid expenses and other | 8 | 22 | 2 |
| | 296 | 780 | 508 |
| **CASH PROVIDED BY (USED FOR) INVESTING** | | | |
| Capital expenditures | (225) | (187) | (192) |
| Reforestation and net acquisition of timber and timberland | (12) | (17) | (28) |
| Sale of timberland | (21) | — | — |
| Sales of non-strategic assets and operations and proceeds from sale of property and equipment | 24 | 64 | 45 |
| Acquisitions, net of cash acquired, and joint ventures | (5) | (148) | (5) |
| Other | 4 | 1 | 2 |
| | (235) | (287) | (178) |
| **CASH PROVIDED BY (USED FOR) FINANCING** | | | |
| Nonrecourse borrowing secured by financial assets of special purpose entities | 2,140 | — | — |
| Payments of debt | (567) | (47) | (502) |
| Borrowings under accounts receivable securitization facility, net | (163) | 133 | 15 |
| Borrowings under revolving credit facility, net | (12) | (56) | — |
| Change in book overdrafts | 13 | 2 | (13) |
| Fees associated with debt | (42) | — | — |
| Other additions to debt | — | 10 | 500 |
| Cash dividends paid to shareholders | (1,212) | (108) | (102) |
| Repurchase of common stock | (24) | (318) | (527) |
| Exercise of options | 20 | 47 | 48 |
| Tax benefit of stock options exercised | 15 | 10 | — |
| Settlement of equity purchase contracts | — | — | 345 |
| Other | — | (4) | (7) |
| | 168 | (331) | (243) |
| **CASH PROVIDED BY (USED FOR) DISCONTINUED OPERATIONS** | | | |
| Net cash provided by (used for) operating activities | (33) | 255 | 78 |
| Net cash provided by (used for) investing activities | (619) | 1,056 | (1,785) |
| Net cash provided by (used for) financing activities | 620 | (1,443) | 1,611 |
| | (32) | (132) | (96) |
| Effect of exchange rate changes on cash and cash equivalents | — | — | — |
| Net increase (decrease) in cash and cash equivalents | 197 | 30 | (9) |
| Cash and cash equivalents at beginning of year | 30 | — | 9 |
| Cash and cash equivalents at year-end | $ 227 | $ 30 | $ — |

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## TEMPLE-INLAND INC. AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

| | Common Stock | Additional Paid-In Capital | Accumulated Other Comprehensive Income / (Loss) | Retained Earnings | Treasury Stock | Total |
|---|---|---|---|---|---|---|
| | | | (In millions) | | | |
| **Balance at year-end 2004** | $123 | $350 | $(192) | $ 2,067 | $(241) | $ 2,107 |
| Comprehensive income, net of tax: | | | | | | |
| Net income | — | — | — | 176 | — | 176 |
| Unrealized gains/(losses) on securities | — | — | (3) | — | — | (3) |
| Defined benefits | — | — | 3 | — | — | 3 |
| Foreign currency translation adjustment | — | — | 4 | — | — | 4 |
| Derivative financial instruments | — | — | (1) | — | — | (1) |
| **Comprehensive income for the year 2005** | | | | | | 179 |
| Dividends paid on common stock — $0.90 per share | — | — | — | (102) | — | (102) |
| Share-based compensation, net of distributions — 578,774 shares | — | 13 | — | — | 19 | 32 |
| Exercise of stock options — 1,833,688 net shares | — | — | — | — | 48 | 48 |
| Tax benefit from exercise of stock options | — | 7 | — | — | — | 7 |
| Settlement of equity purchase contracts — 10,875,739 shares | 1 | 75 | — | — | 269 | 345 |
| Repurchase of common stock — 14,500,000 shares | — | — | — | — | (536) | (536) |
| **Balance at year-end 2005** | $124 | $445 | $(189) | $ 2,141 | $(441) | $ 2,080 |
| Comprehensive income, net of tax: | | | | | | |
| Net income | — | — | — | 468 | — | 468 |
| Unrealized gains/(losses) on securities | — | — | (1) | — | — | (1) |
| Defined benefits | — | — | 57 | — | — | 57 |
| Foreign currency translation adjustment | — | — | (2) | — | — | (2) |
| Derivative financial instruments | — | — | 1 | — | — | 1 |
| **Comprehensive income for the year 2006** | | | | | | 523 |
| Dividends paid on common stock — $1.00 per share | — | — | — | (108) | — | (108) |
| Share-based compensation, net of distributions — 10,289 shares | — | 28 | — | — | (1) | 27 |
| Exercise of stock options — 1,736,335 net shares | — | (15) | — | — | 62 | 47 |
| Tax benefit from exercise of stock options | — | 10 | — | — | — | 10 |
| Repurchase of common stock — 7,850,000 shares | — | — | — | — | (333) | (333) |
| Adoption of SFAS No. 158, net of tax | — | — | (57) | — | — | (57) |
| **Balance at year-end 2006** | $124 | $468 | $(191) | $ 2,501 | $(713) | $ 2,189 |
| Comprehensive income, net of tax: | | | | | | |
| Net income | — | — | — | 1,305 | — | 1,305 |
| Unrealized gains/(losses) on securities | — | — | (36) | — | — | (36) |
| Defined benefits | — | — | 53 | — | — | 53 |
| Foreign currency translation adjustment | — | — | — | — | — | — |
| Derivative financial instruments | — | — | — | — | — | — |
| **Comprehensive income for the year 2007** | | | | | | 1,322 |
| Regular dividends paid on common stock — $1.12 per share | — | — | — | (118) | — | (118) |
| Special dividend paid on common stock — $10.25 per share | — | — | — | (1,094) | — | (1,094) |
| Share-based compensation, net of distributions — 281,472 shares | — | 2 | — | — | 16 | 18 |
| Exercise of stock options — 1,009,246 net shares | — | (10) | — | — | 30 | 20 |
| Tax benefit from exercise of stock options | — | 15 | — | — | — | 15 |
| Adoption of FASB Interpretation No. 48, net of tax | — | — | — | 5 | — | 5 |
| Adoption of measurement provisions of SFAS No. 158, net of tax | — | — | — | (5) | — | (5) |
| Spin-off of Forestar | — | — | — | (434) | — | (434) |
| Spin-off of Guaranty | — | — | 35 | (1,173) | — | (1,138) |
| **Balance at year-end 2007** | $124 | $475 | $(139) | $ 987 | $(667) | $ 780 |

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## TEMPLE-INLAND INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### Note 1 — Summary of Significant Accounting Policies

*Basis of Presentation*

On December 28, 2007, we completed our transformation plan that was approved by our board of directors in February 2007. A summary of the significant elements of the transformation plan follows:

- On October 31, 2007, we sold 1.55 million acres of timberland for $2.38 billion to an investment entity affiliated with The Campbell Group, LLC and recognized a pre-tax gain of $2.053 billion, which is included in other operating income. The acreage sold consisted of 1.38 million acres owned in fee and leases covering 175,000 acres. The total consideration consisted almost entirely of notes due in 2027, which are secured by irrevocable letters of credit issued by independent financial institutions. We also entered into a 20-year fiber supply agreement for pulpwood and a 12-year fiber supply agreement for sawtimber. Both agreements are at market prices, and are subject to extension.

- We contributed the notes and irrevocable letters of credit received in connection with the sale of our timberlands to two wholly-owned, bankruptcy-remote special purpose entities. On December 3, 2007, the special purpose entities pledged the notes receivable from the sale of timberland as collateral for $2.14 billion nonrecourse loans payable 2027. The net cash proceeds, after alternative minimum and other taxes related to sale of the timberland and transaction costs, were $1.8 billion. We used $1.1 billion of the net cash proceeds to pay a $10.25 per share special cash dividend to our shareholders in December 2007. The remaining $700 million was used to reduce debt. We have concluded that we are the primary beneficiary of these special purpose entities. As a result we include these special purpose entities in our consolidated financial statements.

- On December 28, 2007, we completed the spin-off of our real estate segment, Forestar Real Estate Group Inc. (Forestar), and our financial services segment, Guaranty Financial Group Inc. (Guaranty). These spin-offs were effected through tax-free distributions of one share of Forestar and one share of Guaranty for every three shares of Temple-Inland common stock. These spin-offs reduced retained earnings by $1.6 billion. Our financial information has been reclassified to reflect Forestar and Guaranty as discontinued operations for all periods presented.

The transformation plan significantly changed our capital structure and operations. At year-end 2007, Temple-Inland is a manufacturing company focused on corrugated packaging and building products.

Our consolidated financial statements include the accounts of Temple-Inland Inc., its subsidiaries and special purpose and variable interest entities of which we are the primary beneficiary. We account for our investment in other entities in which we have significant influence over operations and financial policies using the equity method.

We prepare our financial statements in accordance with generally accepted accounting principles, which require us to make estimates and assumptions about future events. Actual results can, and probably will, differ from those we currently estimate. We eliminate all material intercompany accounts and transactions.

Our fiscal year ends on the Saturday closest to December 31, which from time to time means that a fiscal year will include 53 weeks instead of 52 weeks. All of the periods presented had 52 weeks. Fiscal year 2007 ended on December 29, 2007, fiscal year 2006 ended on December 30, 2006, and fiscal year 2005 ended on December 31, 2005.

We translate the balance sheets of our international operations where the functional currency is other than the U.S. dollar into U.S. dollars at year-end exchange rates. We include adjustments resulting from financial statement translation in other comprehensive income.

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***Asset Retirement Obligations and Environmental Obligations***

We recognize legal obligations associated with the retirement of long-lived assets when the obligation is incurred. We record the estimated present value of the retirement obligation and increase the carrying value of the long-lived asset by a like amount. Over time, we accrete or increase the liability to its settlement value and we depreciate or decrease the asset to zero. When we settle the obligation we recognize a gain or loss for any difference between the settlement amount and the then recorded obligation. At year-end 2005, we adopted Financial Accounting Standards Board (FASB) Interpretation No. 47, *Accounting for Conditional Asset Retirement Obligations an interpretation of FASB Statement No. 143.* This interpretation clarified that the term "conditional asset retirement obligation" refers to a legal obligation to perform an asset retirement obligation in which the timing and/or method of settlement are conditional on future events that may or may not be within our control. As a result, even though the timing and/or method of settlement may be uncertain, the retirement obligation should be recognized if it can be reasonably estimated. The effect on earnings and financial position of adopting this interpretation was not significant.

Our asset retirement obligations consist principally of costs to remediate landfills we operate. The present value of these asset retirement obligations was $13 million at year-end 2007 and $16 million at year-end 2006 and is included in other long-term liabilities. Accretion expense was less than $1 million in 2007, $1 million in 2006 and less than $1 million in 2005.

Many of our manufacturing facilities contain asbestos and lead paint. We are currently not required to remove any of these materials, but we could be required to do so in the future if we were to demolish or undertake major renovations of these facilities. At this time, we have no such plans, which makes it impractical to estimate the fair value of any related asset retirement obligations. Accordingly, a liability has not been recognized for these asset retirement obligations.

In addition, we record environmental remediation liabilities on an undiscounted basis when environmental assessments or remediation are probable and we can reasonably estimate the cost. We adjust these liabilities as further information is obtained or circumstances change. Accrued remediation liabilities were $13 million at year-end 2007, of which $11 million is included in other accrued expenses and $2 million in other long-term liabilities. At year-end 2006, accrued remediation liabilities were $13 million of which $9 million were included in other accrued expenses, $2 million in other long-term liabilities, and $2 million in liabilities of discontinued operations.

***Capitalized Software***

We capitalize purchased software costs as well as the direct internal and external costs associated with software we develop for our own use. We amortize these capitalized costs using the straight-line method over estimated useful lives ranging from three to seven years. The carrying value of capitalized software was $35 million at year-end 2007 and $46 million at year-end 2006 and is included in other assets. The amortization of these capitalized costs was $15 million in 2007, $17 million in 2006, and $15 million in 2005 and is included in cost of sales and general and administrative expense.

***Cash and Cash Equivalents***

Cash and cash equivalents include cash and other short-term instruments with original maturities of three months or less.

***Derivatives***

We use, from time to time and then only to a limited degree, derivative instruments to mitigate our exposure to risks associated with changes in interest rates, product pricing and manufacturing costs. We do not enter into derivatives for trading purposes. We defer and include in other comprehensive income changes in

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the fair value of derivative instruments designated as cash flow hedges until the hedged transactions are completed. At that time, we recognize these deferred gains or losses in income. We recognize the ineffective portion of these hedges, which is not significant, in income. We recognize changes in the fair value of derivative instruments designated as fair value hedges in income, as well as changes in the fair value of the hedged item. We recognize changes in the fair value of derivative instruments that are not designated as hedges in income. We include the carrying value of derivative instruments in other assets and other liabilities.

Derivative financial instruments are designated and documented as hedges at the inception of the contract and on an ongoing basis. We assess and measure the effectiveness of derivative instruments, using correlation ratios, at inception and on an ongoing basis. If a derivative instrument ceases to be highly effective as a hedge or if the derivative instrument is terminated or settled prior to the expected maturity or realization of the underlying item, we stop using hedge accounting.

***Fair Value of Financial Instruments***

In the absence of quoted market prices, we estimate the fair value of financial instruments. Our estimates are affected by the assumptions we make, including the discount rate and estimates of the amount and timing of future cash flows. Where these fair values approximate carrying value, no separate disclosure of fair value is shown.

***Goodwill and Other Intangible Assets***

We do not amortize goodwill and other indefinite lived intangible assets. Instead, we measure these assets for impairment based on estimated fair values at least annually or more frequently if impairment indicators exist. We perform the annual impairment measurement as of the beginning of the fourth quarter of each year. Intangible assets with finite useful lives are amortized over their estimated lives.

***Impairment of Long-Lived Assets***

We review long-lived assets held for use for impairment when events or circumstances indicate that their carrying value may not be recoverable. Impairment exists if the carrying amount of the long-lived asset is not recoverable from the undiscounted cash flows expected from its use and eventual disposition. We determine the amount of the impairment loss by comparing the carrying value of the long-lived asset to its estimated fair value. In the absence of quoted market prices, we determine estimated fair value generally based on the present value of future probability weighted cash flows expected from the use and eventual disposition of the long-lived asset. We carry assets held for sale at the lower of carrying value or estimated fair value less costs to sell.

***Income Taxes***

We provide deferred income taxes using current tax rates for temporary differences between the financial accounting carrying value of assets and liabilities and their tax accounting carrying values. We recognize and value income tax exposures for the various taxing jurisdictions where we operate based on tax laws, tax elections, commonly accepted tax positions, and management estimates. We include tax penalties and interest in income tax expense.

In 2007, we adopted the provisions of FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes*. As a result of the implementation, we increased assets by $2 million, reduced liabilities by $3 million, and increased beginning retained earnings by $5 million. We also reclassified $11 million from deferred income taxes to other long-term liabilities.

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***Inventories***

We carry inventories at the lower of cost or market. We determine cost using the average cost method, which approximates the first-in, first-out method.

In 2006, we began applying the guidance in Emerging Issues Task Force (EITF) Issue No. 04-13, *Accounting for Purchases and Sales of Inventory with the Same Counterparty*. This guidance requires that non-monetary exchanges of similar inventory be valued at the carrying value of the inventory given up instead of the fair value of the inventory received and is applied to exchange agreements entered into or renewed subsequent to first quarter 2006. Our corrugated packaging segment enters into these agreements that generally represent the exchange of linerboard we manufacture for corrugated medium manufactured by others. We include these exchanges in cost of sales. The effect of applying this guidance was to increase cost of sales $2 million in 2007 and $7 million in 2006.

***Pension and Postretirement Plans***

At year-end 2006 we adopted Statement of Financial Accounting Standards (SFAS) No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans*, requiring the funded status of defined benefit plans be shown on the balance sheet. In 2007, we transitioned to a year-end measurement date for valuing plan assets and obligations for our defined benefit and postretirement benefit plans as further required by SFAS No. 158. Previously we used a measurement date of September 30. Upon transition, we reduced 2007 beginning shareholders' equity by $5 million, representing the net periodic benefit cost of the three month period from the last measurement date to year-end 2006, net of tax, and increased liability for pension benefits.

The following table shows the effect of applying SFAS No. 158 on individual line items in the 2006 consolidated balance sheet:

| | Before Application of SFAS No. 158 | Adjustments Increase (Decrease) | After Application of SFAS No. 158 |
|---|---|---|---|
| | | (In millions) | |
| Prepaid expenses and other | $ 76 | $(16) | $ 60 |
| Deferred tax liability | 279 | (35) | 244 |
| Liability for pension benefits | 156 | 73 | 229 |
| Liability for postretirement benefits | 119 | 3 | 122 |
| Total liabilities | 18,244 | 41 | 18,285 |
| Accumulated other comprehensive loss | 134 | 57 | 191 |
| Total shareholders' equity | 2,246 | (57) | 2,189 |

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***Property and Equipment***

We carry property and equipment at cost less accumulated depreciation. We capitalize the cost of significant additions and improvements, and we expense the cost of repairs and maintenance, including planned major maintenance. We capitalize interest costs incurred on major construction projects. We depreciate these assets using the straight-line method over their estimated useful lives as follows:

| Classification | Estimated Useful Lives | Carrying Value At Year-End 2007 |
|---|---|---|
| | | (In millions) |
| Land and land improvements | N/A | $ 40 |
| Buildings and building improvements | 10 to 40 years | 298 |
| Machinery and equipment: | | |
| Paper machines | 5 to 25 years | 632 |
| Mill equipment | 5 to 25 years | 79 |
| Converting equipment | 3 to 20 years | 410 |
| Other production equipment | 5 to 25 years | 5 |
| Transportation equipment | 3 to 20 years | 28 |
| Office and other equipment | 3 to 5 years | 20 |
| Construction in progress | N/A | 120 |
| | | $1,632 |

We include in property and equipment $57 million of assets subject to capital leases. We depreciate these assets and any improvements to leased assets using the straight-line method over the shorter of their lease term or their estimated useful lives. We expense operating leases ratably over the lease term.

***Revenue Recognition***

We recognize product revenue upon passage of title, which occurs at the time the product is delivered to the customer, the price is fixed and determinable, and we are reasonably sure of collection. Other revenue, which is not significant, is recognized when the service has been performed, the value is determinable, and we are reasonably sure of collection.

We include the amounts billed to customers for shipping in net revenues and the related costs in cost of sales.

We exclude from revenue, amounts we collect from customers that represent sales tax or other taxes that are based on the sale. These amounts are included in other accrued expenses until paid.

***Share-Based Compensation***

Beginning January 2006, we adopted the modified prospective application method contained in SFAS No. 123 (revised December 2004), *Share-Based Payment* (SFAS 123(R)), to account for share-based payments. As a result, we apply this pronouncement to new awards or modifications of existing awards in 2006 and thereafter. We had been expensing over the service period the fair value of share-based compensation awards granted, modified or settled in 2003 through 2005, using the prospective transition method of accounting contained in SFAS No. 148, *Accounting for Stock-Based Compensation-Transition and Disclosure, an amendment of FASB Statement No. 123*. The principal effects of adopting SFAS 123(R) are:

- The fair value of awards granted to retirement eligible employees is expensed at the date of grant because our stock option awards and some of our other awards provide for accelerated or continued

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vesting upon retirement. Previously, the fair value of these awards was expensed over the expected service period. This change accelerated about $6 million of expense into first quarter 2006 related to awards granted in 2006. We will continue to expense the fair value of awards granted prior to 2006 over the expected service period.

- Forfeitures over the expected term of the award are estimated at the date of grant and the estimates adjusted to reflect actual subsequent forfeitures. Previously, we had reflected forfeitures as they occurred. The effect of this change was not significant.
- Tax benefits recognized as a result of the exercise of employee stock options are classified as a financing cash flow. Prior to 2006, we classified these tax benefits as an operating cash flow.
- The fair value of unvested outstanding options at the beginning of first quarter 2006 will be expensed over the remaining service period. The effect of this change was not significant because we began accounting for options at fair value determined at the date of grant in 2003. As a result, this applied only to our unvested outstanding options granted prior to 2003.

Adoption of this new pronouncement did not change the methodology we use to determine the fair value of our share-based compensation arrangements. We use the Black-Scholes-Merton option-pricing model for stock options and the grant date or period-end fair value of our common stock for all other awards.

Prior to 2003, we used the intrinsic value method in accounting for stock options. As a result, no share-based compensation expense related to those stock options granted prior to 2003 is reflected in net income for 2005. The following table illustrates the effect on net income and earnings per share as if the fair value method had been applied to all options granted.

| | For the Year 2005 (In millions, except per share) |
|---|---|
| Net income, as reported | $ 176 |
| Add: Share-based compensation expense, net of related tax effects, included in the determination of reported net income[a] | 19 |
| Deduct: Total share-based compensation expense, net of related tax effects, determined under the fair value based method for all awards[a] | (23) |
| Pro forma net income | $ 172 |
| Earnings per share | |
| Basic, as reported | $1.56 |
| Basic, pro forma | $1.53 |
| Diluted, as reported | $1.54 |
| Diluted, pro forma | $1.50 |

[a] Includes treasury stock contributions to fulfill our obligation for matching contributions to our 401(k) plans of $3 million, net of related tax effects.

***Special Purpose and Variable Interest Entities***

We account for special purpose and variable interest entities using FASB Interpretation No. 46 (revised December 2003), *Consolidation of Variable Interest Entities an Interpretation of ARB No. 51*. This interpretation provides guidance for determining whether an entity is a variable interest entity and which beneficiary of the variable interest entity, if any, should consolidate the variable interest entity.

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***Timber and Timberland***

In 2007, we sold all of our strategic timber and timberland.

We carried timber and timberland at cost, less the cost of timber cut. We capitalized the costs we paid to purchase timber and timberland, and we allocated that cost to the timber, timberland, and if applicable, mineral rights, based on estimated relative fair values, which in the case of significant purchases, we based on third-party appraisals.

We expensed the cost of timber cut based on the relationship of the timber carrying value to the estimated volume of recoverable timber multiplied by the amount of timber cut. We included the cost of timber cut in depreciation expense. We determined the estimated volume of recoverable timber using statistical information and other data related to growth rates and yields gathered from physical observations, models, and other information gathering techniques. Changes in yields were generally due to adjustments in growth rates and similar matters and were accounted for prospectively as changes in estimates. We capitalized reforestation costs incurred in developing viable seedling plantations (up to two years from planting), such as site preparation, seedlings, planting, fertilization, insect and wildlife control, and herbicide application. We expensed all other costs, such as property taxes and costs of forest management personnel, as incurred. Once the seedling plantation was viable, we expensed all costs to maintain the viable plantations, such as fertilization, herbicide application, insect and wildlife control, and thinning, as incurred. We capitalized costs incurred to initially build roads as land improvements, and we expensed as incurred costs to maintain these roads.

We determined the carrying value of timberland sold using the area method by county, which was based on the relationship of carrying value of timberland to total acres of timberland multiplied by acres of timberland sold. We determined the carrying value of timber sold by the average cost method, which was based on the relationship of timber carrying value to the estimate of recoverable timber multiplied by the amount of timber sold.

***Pending Accounting Pronouncements***

SFAS No. 141(R), *Business Combinations* — This new standard requires most identifiable assets, liabilities, noncontrolling interests, and goodwill acquired in a business combination to be recorded at full fair value. The new standard also changes the approach to determining the purchase price; the accounting for acquisition cost; and the accounting practices for acquired contingencies, restructuring costs, long-lived assets, in-process research and development, share-based payment awards, indemnification costs, and tax benefits. SFAS No. 141(R) is effective for any business combination occurring after our year-end 2008.

SFAS No. 157, *Fair Value Measures* — This standard defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. This guidance applies to fair value measurements already required or permitted and will be effective for our first quarter 2008. We do not expect that adoption will have a significant effect on our earnings or financial position.

SFAS No. 159, *The Fair Value Options for Financial Assets and Financial Liabilities* — This standard permits the election of fair value as the initial and subsequent measurement method for many financial assets and liabilities. Subsequent changes in the fair value would be recognized in earnings as they occur. Electing the fair value option requires the disclosure of the fair value of affected assets and liabilities on the balance sheet or in the notes to the financial statements. SFAS No. 159 is effective for our first quarter 2008. We do not anticipate electing this option.

SFAS No. 160, *Noncontrolling Interest in Consolidated Financial Statements* — This new standard specifies that noncontrolling interests be reported as a part of equity, not as a liability or other item outside of

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equity. SFAS No. 160 is effective for our first quarter 2009. Based on our current understanding, we do not expect that adoption will have a significant effect on our earnings or financial position.

## Note 2 — Acquisitions

In 2006, we purchased for $150 million our partner's 50 percent interest in Standard Gypsum LP, which manufactured and sold gypsum wallboard. We also paid off the partnership's $56 million credit agreement, of which $28 million related to the purchased interest. We financed this purchase with borrowings under our revolving credit facilities. We believe that this acquisition will allow us to continue to generate earnings and returns from our gypsum wallboard operations, as these operations are low cost and are located near fast growing markets.

We no longer maintain Standard Gypsum as a separate legal entity and include all of its assets and liabilities, results of operations, and cash flows in our consolidated financial statements. Previously we had accounted for our interest in Standard Gypsum using the equity method. We allocated the purchase price to the 50 percent of the assets acquired and liabilities assumed based on our estimates of their fair value at the date of acquisition. We based these estimates of fair values on independent appraisals and other information. Goodwill is allocated to the building products segment, and we anticipate that all of the goodwill will be deductible for income tax purposes. The other 50 percent of the assets and liabilities, which we already owned, were included at their carrying value.

A summary of the net assets at the date of acquisition (50 percent at fair value and 50 percent at carrying value) follows:

| | Total (In millions) |
|---|---|
| Current assets | $ 35 |
| Property and equipment | 74 |
| Goodwill | 129 |
| Total assets | 238 |
| Current liabilities | (13) |
| Current portion of long-term debt | (56) |
| Total liabilities | (69) |
| Net assets at date of acquisition | $169 |

Unaudited pro forma information assuming this acquisition and related financing had occurred at the beginning of 2005 would have resulted in revenues of $4.04 billion, income from continuing operations of $32 million, and income from continuing operations per diluted share of $0.28.

We derived these pro forma results by adjusting for the effects of the purchase price allocations and financing described above. These pro forma results are not necessarily an indication of what would have occurred if the acquisition and financing had been completed at the beginning of 2005 and are not intended to be indicative of future results.

## Note 3 — Joint Ventures

Our significant manufacturing joint venture investments at year-end 2007 are: Premier Boxboard Limited LLC, a 50 percent owned venture that produces gypsum facing paper and corrugating medium in Newport, Indiana , and Del-Tin Fiber LLC, a 50 percent owned venture that produces medium density fiberboard in El Dorado, Arkansas.. The joint venture partner in each of these ventures is a publicly-held company unrelated to us. In January 2006, we purchased our partner's 50 percent interest in Standard Gypsum LP. As a result,

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beginning in 2006, we include all of its assets and liabilities, results of operations, and cash flow in our consolidated financial statements. Please read **Note 2** for additional information.

Combined summarized financial information for these joint ventures follows:

| | At Year-End | |
|---|---|---|
| | 2007 | 2006 |
| | (In millions) | |
| Current assets | $ 29 | $ 26 |
| Total assets | 234 | 241 |
| Current liabilities[(a)] | 25 | 24 |
| Long-term debt | 85 | 90 |
| Equity | 124 | 127 |
| Our investment in joint ventures: | | |
| 50 percent share in joint ventures' equity | $ 62 | $ 63 |
| Unamortized basis difference | (30) | (32) |
| Investment in joint ventures | $ 32 | $ 31 |

(a) Includes current maturities of debt of $6 million in 2007 and $6 million in 2006.

| | For the Year | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| | (In millions) | | |
| Net revenues | $200 | $192 | $378 |
| Operating income | 13 | 24 | 85 |
| Earnings | 5 | 17 | 74 |
| Our equity in earnings: | | | |
| 50 percent share of earnings | $ 3 | $ 8 | $ 37 |
| Amortization of basis difference | 2 | 3 | 2 |
| Equity in earnings of joint ventures | $ 5 | $ 11 | $ 39 |

We and our joint venture partners contribute to these ventures and receive distributions from them equally. In 2007, we contributed $4 million to these ventures and received $8 million in distributions, in 2006 we contributed $3 million and received $12 million in distributions, and in 2005 we contributed $5 million and received $43 million in distributions.

Our investment in these joint ventures is included in other assets, and our equity in their earnings is included in other operating income (expense). Our investment in and our equity in their earnings differs from our 50 percent interest due to the difference between the fair value of net assets contributed to the Premier Boxboard joint venture and our carrying value of those assets. When we contributed the Newport, Indiana mill and its associated debt to the Premier Boxboard joint venture in 2000, the fair value of the net assets exceeded our carrying value by $55 million. The joint venture recorded the contributed assets at fair value. We did not recognize a gain as a result of the contribution of assets, thus creating a difference in the carrying value of our investment and our underlying equity in the venture. We are amortizing this difference over the same period as the underlying mill assets are being depreciated by the joint venture to reflect depreciation of the mill as if it were consolidated by us at its historical carrying value. At year-end 2007, the unamortized basis difference was $30 million.

We provide marketing services to the Del-Tin joint venture, and prior to 2006, we provided marketing and management services to the Standard Gypsum joint venture. Fees for these services were $2 million in 2007, $3 million in 2006, and $8 million in 2005 and are included as a reduction of cost of sales and selling

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expense. We also purchase, at market rates, finished products from the Premier Boxboard joint venture, which aggregated $47 million in 2007, $62 million in 2006, and $40 million in 2005.

In 2005, we sold about 7,000 acres of timber and timberland to a joint venture in which our former real estate segment owned 50 percent and an unrelated public company owned the other 50 percent. This acreage was sold pursuant to the terms of a long-standing option agreement, which was about to expire. The joint venture intended to hold the land for future development and sale. We recognized about half of the $10 million gain in income in 2005 and recognized the remainder in 2007 when we spun off our real estate segment.

### Note 4 — Long-Term Debt

Long-term debt consists of:

| | At Year-End | |
|---|---|---|
| | 2007 | 2006 |
| | (In millions) | |
| Borrowings under bank credit agreements — average interest rate of 6.26% in 2007 and 5.89% in 2006 | $ — | $ 12 |
| Accounts receivable securitization facility — average interest rate of 5.44% in 2007 and 5.05% in 2006 | 1 | 164 |
| 6.75% Notes, payable in 2009 | 14 | 300 |
| 7.875% Senior Notes, payable in 2012, net of discounts | 285 | 498 |
| 6.375% Senior Notes, payable in 2016, net of discounts | 249 | 249 |
| 6.625% Senior Notes, payable in 2018, net of discounts | 248 | 248 |
| Revenue bonds, payable 2007 through 2024 — average interest rate of 5.41% in 2007 and 5.75% in 2006 | 51 | 65 |
| Other indebtedness due through 2027 — average interest rate of 7.89% in 2007 and 6.99% in 2006 | 7 | 61 |
| | 855 | 1,597 |
| Less current portion of long-term debt | (3) | (13) |
| | $852 | $1,584 |

At year-end 2007, we had $835 million in committed credit agreements. These committed agreements include a $750 million credit agreement that expires in 2011. The remaining $85 million of credit agreements expire between 2008 and 2010. At year-end 2007, our unused capacity under these facilities was $821 million.

At year-end 2007, we had a $250 million accounts receivable securitization facility that expires in 2010. Under this facility, a wholly-owned, bankruptcy-remote subsidiary purchases, on an on-going basis, substantially all our trade receivables. As we need funds, the subsidiary draws under its revolving credit arrangement, pledges the trade receivables as collateral, and remits the proceeds to us. In the event of liquidation of the subsidiary, its creditors would be entitled to satisfy their claims from the subsidiary's assets prior to distributions back to us. At year-end 2007, the subsidiary owned $361 million in net trade receivables against which it had borrowed $1 million under this facility. At year-end 2007, the unused capacity under this facility was $246 million. We include this subsidiary in our consolidated financial statements.

Maturities of our debt during the next five years are (in millions): 2008 — $3; 2009 — $33; 2010 — $2; 2011 — $11; 2012 — $293; and thereafter — $513. We have classified $10 million of 2008 stated maturities as long-term based on our intent and ability to refinance them on a long-term basis.

In December 2007, we completed a cash tender offer for $286 million of 6.75% Notes payable in 2009 and $213 million of 7.875% Senior Notes payable in 2012. We incurred $40 million in costs related to these tender offers, which was included in other non-operating (income) expense.

In December 2005, we completed a cash tender offer for $425 million of debt. We incurred $6 million in costs related to this tender offer, which was included in other non-operating (income) expense.

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We capitalized and deducted from interest expense interest incurred on major construction and information technology projects of $1 million in 2007, $1 million in 2006, and $1 million in 2005. We paid interest of $125 million in 2007, $106 million in 2006, and $109 million in 2005.

**Note 5 — Financial Assets and Nonrecourse Financial Liabilities of Special Purpose Entities**

In October 2007, we received $2.38 billion in notes from the sale of 1.55 million acres of timberland, which we contributed to two wholly-owned, bankruptcy-remote special purpose entities. The notes are secured by irrevocable letters of credit, are due in 2027, and require quarterly interest payments based on variable interest rates that reset quarterly (4.98 percent at year-end 2007).

In December 2007, the special purpose entities pledged the notes and irrevocable letters of credit to secure $2.14 billion nonrecourse loans payable in 2027. These borrowings require quarterly interest payments based on variable interest rates that reset quarterly (5.67 percent at year-end 2007).

We include these special purpose entities in our consolidated financial statements.

**Note 6 — Capital Stock**

From February 2005 through year-end 2007, our Board of Directors approved repurchase programs aggregating 29.0 million shares. As of year-end 2007, we had repurchased 22.4 million shares under these programs. In 2007, we initiated no share purchases , but we settled $24 million of share purchases that were initiated in fourth quarter 2006. As of year-end 2007, there are 6.6 million shares remaining under current repurchase authorizations.

Pursuant to the Shareholder Rights Plan, each share of common stock outstanding is coupled with one-quarter of a preferred stock purchase right (Right). Each Right entitles our shareholders to purchase, under certain conditions, one one-hundredth of a share of newly issued Series A Junior Participating Preferred Stock at an exercise price of $200. Rights will be exercisable only if someone acquires beneficial ownership of 20 percent or more of our common shares or commences a tender or exchange offer, upon consummation of which they would beneficially own 25 percent or more of our common shares. We will generally be entitled to redeem the Rights at $0.01 per Right at any time until the 10th business day following public announcement that a 20 percent position has been acquired. The Rights will expire on February 20, 2009.

Please read **Note 9** for information about additional shares of common stock that could be issued under terms of our share-based compensation plans.

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## Note 7 — Accumulated Other Comprehensive Income (Loss)

The components of and changes in accumulated other comprehensive income (loss) were:

| | Unrealized Gains (Losses) on Available-For-Sale Securities | Defined Benefit Plans | Foreign Currency Translation Adjustment | Derivative Instruments | Total |
|---|---|---|---|---|---|
| | | | (In millions) | | |
| Balance at beginning of year 2005 | $ 5 | $(171) | $(26) | $— | $(192) |
| Changes during the year | (4) | 6 | 4 | (1) | 5 |
| Deferred taxes on changes | 1 | (3) | — | — | (2) |
| Net change for 2005 | (3) | 3 | 4 | (1) | 3 |
| Balance at year-end 2005 | $ 2 | $(168) | $(22) | $(1) | $(189) |
| Changes during the year | (1) | 95 | (2) | 1 | 93 |
| Deferred taxes on changes | — | (38) | — | — | (38) |
| Net change for 2006 | (1) | 57 | (2) | 1 | 55 |
| Adoption of SFAS No. 158, net of deferred taxes of $35 | — | (57) | — | — | (57) |
| Balance at year-end 2006 | $ 1 | $(168) | $(24) | $— | $(191) |
| Changes during the year | (56) | 85 | — | — | 29 |
| Deferred taxes on changes | 20 | (32) | — | — | (12) |
| Net change for 2007 | (36) | 53 | — | — | 17 |
| Spin-off of Guaranty | 35 | — | — | — | 35 |
| Balance at year-end 2007 | $ — | $(115) | $(24) | $— | $(139) |

## Note 8 — Pension and Postretirement Plans

The annual expense of our benefit plans consists of:

| | For the Year | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| | (In millions) | | |
| 401 (k) matching plan | $17 | $16 | $16 |
| Defined benefit | 35 | 46 | 49 |
| Postretirement medical | 8 | 9 | 8 |
| | $60 | $71 | $73 |

Our 401(k) matching plan covers substantially all employees and is fully funded.

Our defined benefit plan covers substantially all salaried and hourly employees. Salaried and nonunion hourly employee benefits are based on compensation and years of service, while union hourly plans are based on negotiated benefits and years of service. Our policy is to fund our qualified defined benefit plan on an actuarial basis to accumulate assets sufficient to meet the benefits to be paid in accordance with ERISA requirements. However, from time to time we may make voluntary, discretionary contributions. Our supplemental defined benefit plan is unfunded.

Our postretirement medical plan provides medical benefits to eligible salaried and hourly employees who begin drawing retirement benefits immediately after termination of employment. Our postretirement plan

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provides for medical coverage, including a prescription drug subsidy, for certain participants. Our postretirement plan is funded to the extent of benefit payments.

Additional information about our defined benefit and postretirement medical plans follows.

**Obligations and Funded Status**

Beginning in 2007, we measure the defined benefit and postretirement medical plans benefit obligation, value plan assets, and determine funded status and annual expense at year end. Prior to 2007, we used September 30 as our measurement date. The projected benefit obligation of our defined benefit plan represents the present value of benefits earned adjusted for projected future compensation increases to the date of retirement. The accumulated postretirement benefit obligation of our postretirement benefits plan represents the present value of benefits attributable to employee service periods. The projected benefit obligation and the accumulated postretirement benefit obligation are collectively referred to as benefit obligation. The fair value of plan assets represents the fair value, generally market value at the measurement date, of all plan assets. The funded status for the plans represents the difference between the benefit obligation and the fair value of the plan assets.

A summary of the changes in the benefit obligation, plan assets, and funded status follows:

| | For the Year | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Defined Benefits | | | | | | Postretirement Benefits | |
| | Qualified | | Supplemental | | Total | | | |
| | 2007 | 2006 | 2007 | 2006 | 2007 | 2006 | 2007 | 2006 |
| | (In millions) | | | | | | | |
| Benefit obligation — beginning of valuation period | $(1,284) | $(1,300) | $(56) | $(51) | $(1,340) | $(1,351) | $(139) | $(155) |
| Service cost | (32) | (27) | (1) | (1) | (33) | (28) | (2) | (2) |
| Interest cost | (94) | (71) | (4) | (2) | (98) | (73) | (10) | (8) |
| Plan amendments | — | (1) | — | — | — | (1) | — | — |
| Actuarial gain (loss) | 16 | 51 | (4) | (4) | 12 | 47 | (3) | 11 |
| Benefits paid by the plan | 84 | 64 | 6 | 2 | 90 | 66 | 21 | 18 |
| Participant contributions | — | — | — | — | — | — | (4) | (3) |
| Benefit obligation — end of valuation period | (1,310) | (1,284) | (59) | (56) | (1,369) | (1,340) | (137) | (139) |
| Fair value of plan assets — beginning of valuation period | 1,094 | 1,004 | — | — | 1,094 | 1,004 | — | — |
| Actual return | 165 | 94 | — | — | 165 | 94 | — | — |
| Benefits paid by the plan | (84) | (64) | (6) | (2) | (90) | (66) | (21) | (19) |
| Contributions we made | 75 | 60 | 6 | 2 | 81 | 62 | 17 | 16 |
| Participant contributions | — | — | — | — | — | — | 4 | 3 |
| Fair value of plan assets — end of valuation period | 1,250 | 1,094 | — | — | 1,250 | 1,094 | — | — |
| Funded status — end of valuation period | (60) | (190) | (59) | (56) | (119) | (246) | (137) | (139) |
| Contributions we made after the annual measurement date | — | 15 | — | — | — | 15 | — | 4 |
| Funded status at year-end | $ (60) | $ (175) | $(59) | $(56) | $ (119) | $ (231) | $(137) | $(135) |

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Assets and (liabilities) included in the consolidated balance sheet and a reconciliation to funded status follows:

| | At Year-End | | | |
|---|---|---|---|---|
| | Defined Benefits | | Postretirement Benefits | |
| | 2007 | 2006 | 2007 | 2006 |
| | (In millions) | | | |
| Liability/funded status | $(119) | $(231) | $(137) | $(135) |
| Accumulated other comprehensive loss: | | | | |
| Unrecognized net loss | $ 166 | $ 253 | $ 21 | $ 19 |
| Unamortized prior service cost | 13 | 16 | (13) | (16) |
| Additional minimum liability | — | — | — | — |
| Total accumulated other comprehensive loss | $ 179 | $ 269 | $ 8 | $ 3 |

## Additional Information

The accumulated benefit obligation of our defined benefit plan represents the present value of benefits earned without regard to projected future compensation increases. Our defined benefit plans have accumulated benefit obligations in excess of plan assets as follows:

| | At Year-End | |
|---|---|---|
| | 2007 | 2006 |
| | (In millions) | |
| Projected benefit obligation | $(1,369) | $(1,340) |
| Accumulated benefit obligation | $(1,305) | $(1,267) |
| Fair value of plan assets | 1,250 | 1,094 |
| Contributions we made after the annual measurement date | — | 15 |
| Excess of accumulated benefit obligation over fair value of plan assets | $ (55) | $ (158) |
| Excess of accumulated benefit obligation over fair value of plan assets consists of: | | |
| Qualified plan | $ (1) | $ (108) |
| Supplemental plan | (54) | (50) |
| | $ (55) | $ (158) |

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**Components of Net Periodic Benefit Expense and Other Amounts Recognized in Other Comprehensive Income**

| | For the Year | | | | | |
|---|---|---|---|---|---|---|
| | Defined Benefits | | | Postretirement Benefits | | |
| | 2007 | 2006 | 2005 | 2007 | 2006 | 2005 |
| | (In millions) | | | | | |
| Net periodic benefit expense: | | | | | | |
| Service costs — benefits earned during the period | $ 27 | $ 28 | $ 25 | $ 1 | $ 2 | $ 2 |
| Interest cost on benefit obligation | 78 | 73 | 72 | 8 | 8 | 8 |
| Expected return on plan assets | (85) | (78) | (72) | — | — | — |
| Amortization of prior service costs | 2 | 2 | 2 | (2) | (2) | (2) |
| Amortization of actuarial net loss | 14 | 22 | 23 | 1 | 1 | — |
| Total net periodic benefit expense[(a)] | 36 | 47 | 50 | 8 | 9 | 8 |
| Amounts recognized in other comprehensive income, pre-tax | (90) | (95) | (6) | 5 | — | — |
| Total recognized in net periodic benefit expense and other comprehensive income, pre-tax | $(54) | $(48) | $ 44 | $13 | $ 9 | $ 8 |

(a) Includes amounts allocated to discontinued operations of $1 million in 2007, 2006, and 2005.

We estimate that our 2008 net periodic pension expense will be about $37 million. In addition, we expect a one-time expense of $15 million in 2008 related to lump-sum settlements of supplemental benefits. The 2008 net periodic pension expense includes $5 million of net loss and $6 million of prior service cost that will be amortized from accumulated other comprehensive loss. We estimate that our 2008 net periodic postretirement expense will be about $8 million, which includes $1 million of net loss that will be amortized from accumulated other comprehensive loss and a credit of $2 million for prior service cost that will be amortized from a gain component of the net accumulated other comprehensive loss.

**Assumptions**

The assumptions we used to determine defined benefit obligations were:

| | Defined Benefits | | Postretirement Benefits | |
|---|---|---|---|---|
| | 2007 | 2006 | 2007 | 2006 |
| Discount rate | 6.125% | 6.00% | 6.125% | 6.00% |
| Rate of compensation increase | 3.70% | 3.80% | — | — |

The assumptions we used to determine annual net periodic benefit expense were:

| | Defined Benefits | | | Postretirement Benefits | | |
|---|---|---|---|---|---|---|
| | 2007 | 2006 | 2005 | 2007 | 2006 | 2005 |
| Discount rate | 6.00% | 5.50% | 6.00% | 6.00% | 5.50% | 6.00% |
| Expected return on plan assets | 8.00% | 8.00% | 8.50% | — | — | — |
| Rate of compensation increase | 3.80% | 3.70% | 3.70% | — | — | — |

The discount rate is used to determine the present value of the benefit obligations. To arrive at this rate for 2007, we used the December one-month average of the Moody's AA corporate bond rate adjusted to reflect the effect of compounding and for 2006, we used the September one-month average. We believe that this rate is a reasonable proxy for the rate necessary to accumulate funds required to pay the benefits when due.

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The expected long-term rate of return on plan assets is an assumption we make reflecting the anticipated weighted average rate of earnings on the plan assets over the long-term. To arrive at this rate, we developed estimates of the key components underlying capital asset returns including: market-based estimates of inflation, real risk-free rates of return, yield curve structure, credit risk premiums, and equity risk premiums. As appropriate, these components were used to develop benchmark estimates of expected long-term rates of return for each asset class, which were portfolio weighted. Our actual return on plan assets was 9.8 percent in 2007, 10.0 percent in 2006, and 15.0 percent in 2005.

We used the 1994 Group Annuity Mortality Tables to determine benefit obligations and annual defined benefit expense.

The assumed health care cost trend rates we used to determine the expense of the postretirement benefit plans were:

| | For the Year | |
|---|---|---|
| | 2007 | 2006 |
| Health care trend rate assumed for the next year | 9.0% | 8.0% |
| Rate to which the cost trend rate is assumed to decline (ultimate trend rate) | 4.5% | 4.5% |
| Year that the rate reaches the ultimate trend rate | 2014 | 2013 |

These assumed health care cost trend rates have a significant effect on the amounts reported for the postretirement benefit plans. For example, a one-percentage-point change in assumed health care cost trend rates would have the following effect:

| | 1 Percentage Point Increase | 1 Percentage Point Decrease |
|---|---|---|
| | (In millions) | |
| Increase (decrease) in: | | |
| Total service and interest cost components | $ 1 | $(1) |
| Accumulated postretirement benefit obligation | 11 | (9) |

**Plan Assets**

Our defined benefit investment strategies have been developed as part of a comprehensive asset/liability management process that considers the interaction between both assets and liabilities of the plan. These strategies consider not only the expected risk and returns on plan assets, but also the detailed actuarial projections of liabilities as well as plan-level objectives such as projected contributions, expense, and funded status.

In prior years, our principal pension investment strategies included asset allocation and active asset management. The range of target asset allocations was determined after giving consideration to the expected returns of each asset class, the expected variability or volatility of the asset class returns over time, and the complementary nature or correlation of the asset classes within the portfolio. The strategy also employed an active management approach for the portfolio. Each asset class was managed by one or more external money managers with the objective of generating returns, net of management fees that exceed market-based benchmarks.

In the last two months of 2007, we made significant changes to our asset allocation to a more matched position between our assets and liabilities in our qualified defined benefit plan. This action is expected to reduce the volatility of our defined benefit expense and our funding requirements. As shown in the following table, we have moved to an 80 percent asset allocation of debt securities. This portfolio of debt securities has a duration that we believe reasonably approximates our benefit obligation. The remaining 20 percent asset

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allocation (15 percent equity securities; 5 percent real estate) provides market exposure to help mitigate the effects of inflation risk, mortality risk and actuarial risk.

The defined benefit plan weighted-average asset allocations and the range of target allocations follow:

| | Range of Target Allocations | | Percentage of Plan Assets at Year-End | |
|---|---|---|---|---|
| | 2007 | 2006 | 2007 | 2006 |
| Asset category: | | | | |
| Debt securities | 78-88% | 33-37% | 80% | 35% |
| Equity securities | 10-15% | 50-61% | 15 | 59 |
| Real estate | 0-7% | 0-7% | 5 | 6 |
| | | | 100% | 100% |

Equity securities include 591,896 shares of Temple-Inland common stock totaling $12 million or one percent of total plan assets at year-end 2007 and $31 million or three percent of total plan assets as of the 2006 measurement date.

### Cash Flows

We expect our 2008 voluntary, discretionary contributions to our defined benefit plan to approximate 2008 service cost, which is estimated to be about $30 million. We have no minimum 2008 funding requirement under ERISA. Beginning in 2008, benefits earned under the supplemental defined benefit plan will be paid upon retirement or when the employee terminates. In addition, existing retirees were given the option to receive, in January 2008, a lump-sum settlement of supplemental benefits earned. We expect to make lump-sum settlement payments of $42 million in 2008.

The postretirement benefit plan is not subject to minimum regulatory funding requirements. Since the postretirement benefit plans are unfunded, the expected $13 million contribution represents the estimated health claims to be paid for plan participants, net of retiree contributions in 2008.

At year-end 2007, the plans are expected to make the following benefit payments over the next ten years:

| | Defined Benefits | | Postretirement Benefits |
|---|---|---|---|
| | Qualified | Supplemental | |
| | | (In millions) | |
| 2008[a] | $ 72 | $49 | $13 |
| 2009 | 75 | 6 | 12 |
| 2010 | 78 | 6 | 12 |
| 2011 | 82 | 5 | 12 |
| 2012 | 85 | 5 | 12 |
| 2013-2017 | 470 | 17 | 56 |

[a] Includes $42 million in lump-sum settlements in the supplemental plan.

### Note 9 — Share-Based Compensation

We have shareholder approved share-based compensation plans that permit awards to key employees and non-employee directors in the form of restricted or performance units, restricted stock, or options to purchase shares of our common stock. As a result of the spin-off of Forestar and Guaranty, all outstanding share-based awards were equitably adjusted into three separate awards: one related to Temple-Inland common stock, one

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related to Forestar common stock, and one related to Guaranty common stock. The adjustment was made so that immediately following the spin-off, the number of shares relating to each award were adjusted to reflect the distribution ratios and, for options, the per share option exercise price of the original award, was proportionally allocated between Temple-Inland, Forestar, and Guaranty awards based on relative per share trading prices of their common stock immediately following the spin-off. All awards issued as part of this adjustment and the Temple-Inland awards will continue to be subject to their original vesting schedules. Share-based compensation expense on awards held by employees of Temple-Inland will be based on the original grant date fair value for share settled awards, the original grant date Black-Scholes-Merton value for stock option awards, and the sum of the period-end market prices (adjusted for the distribution ratios) of the three companies stock for cash settled awards. After the spin-off, Forestar and Guaranty employees no longer participate in our share-based compensation plans.

We generally grant awards annually in February, and we use treasury stock to fulfill awards settled in common stock and stock option exercises. A summary of these plans follows:

**Restricted or performance units**

Restricted or performance units generally have a three-year term; vest after three years from the date of grant or the attainment of stated ROI based performance goals, generally measured over a three-year period; and are settled in cash or common stock as determined on the date of grant. The restricted and performance units provide for accelerated vesting upon retirement, death, disability, or if there is a change in control. We also have director awards and bonus deferral plans that can be settled in cash or stock. A summary of activity for 2007 follows:

| | Units | Weighted Average Grant Date Fair Value per Unit | Aggregate Current Value |
|---|---|---|---|
| | (In thousands) | | (In millions) |
| Not vested beginning of 2007 | 1,408 | $39 | |
| Granted | 949 | 52 | |
| Vested | (539) | 30 | |
| Forfeited | (16) | 44 | |
| Awards held by Forestar employees at date of spin-off | (121) | 50 | |
| Awards held by Guaranty employees at date of spin-off | (265) | 49 | |
| Not vested year-end 2007 | 1,416 | 48 | $43 |
| Not vested year-end 2007 to be settled in cash and subject to: | | | |
| Time vesting requirements | 711 | | $22 |
| Performance requirements | 705 | | 21 |
| | 1,416 | | $43 |

The fair value of units vested was $26 million in 2007, less than $1 million in 2006, and $1 million in 2005. The fair value of units vested and to be settled in cash was $26 million at year-end 2007 of which $4 million is included in other current liabilities and $22 million is included in long-term liabilities. The fair value of awards settled in cash in 2007 was less than $1 million. There were no awards settled in cash in 2006 or 2005.

**Restricted stock**

Restricted stock awards generally vest after three to six years, and provide for accelerated vesting upon retirement, death, disability, or if there is a change in control. Compensation costs are recognized ratably over the service period. There were no restricted stock awards granted in 2007. There were 435,600 restricted stock

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awards outstanding at year-end 2007 with a weighted average grant date fair value of $33 per share and an aggregate current value of $13 million or $30 per share. The fair value of restricted stock vested in 2007 was $4 million.

**Stock options**

Stock options have a ten-year term, generally become exercisable ratably over four years and provide for accelerated or continued vesting upon retirement, death, disability, or if there is a change in control. Options are granted with an exercise price equal to the market value of our common stock on the date of grant. In addition to the equitable adjustments related to the Forestar and Guaranty spin-offs, the exercise price of all stock option awards was equitably adjusted by $9.85 per share to reflect the effect of the special cash dividend paid in December 2007. The adjustment was based on the difference between the closing price on the day before the stock traded ex-dividend and the opening price on the day the stock began trading ex-dividend. A summary of our activity for 2007 follows:

| | Shares | Weighted Average Exercise Price per Share[(a)] | Weighted Average Remaining Contractual Term | Aggregate Intrinsic Value (Current value less exercise price) |
|---|---|---|---|---|
| | (In thousands) | | (In years) | (In millions) |
| Outstanding beginning of 2007 | 6,012 | $15 | | |
| Granted | 1,028 | 25 | | |
| Exercised | (1,057) | 21 | | |
| Forfeited | (35) | 40 | | |
| Awards held by Forestar employees at date of spin-off | (266) | 17 | | |
| Awards held by Guaranty employees at date of spin-off | (971) | 17 | | |
| Outstanding year-end 2007 | 4,711 | 15 | 6 | $14 |
| Exercisable year-end 2007 | 2,889 | 12 | 4 | $19 |

(a) The weighted average exercise price per share has been adjusted to reflect the spin-off of Forestar and Guaranty, and the special cash dividend.

The intrinsic value of options exercised was $29 million in 2007, $31 million in 2006, and $24 million in 2005.

We estimated the fair value of the options granted using the Black-Scholes-Merton option-pricing model and the following assumptions:

| | For the Year | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| Expected dividend yield | 2.3% | 2.4% | 2.3% |
| Expected stock price volatility | 22.8% | 25.1% | 28.2% |
| Risk-free interest rate | 4.9% | 4.4% | 4.2% |
| Expected life of options in years | 6 | 6 | 8 |
| Weighted average estimated fair value of options granted adjusted for spin-offs: | | | |
| Temple-Inland options | $ 7.39 | $ 6.82 | $ 6.61 |
| Forestar options | 3.09 | 2.85 | 2.77 |
| Guaranty options | 1.99 | 1.83 | 1.77 |
| Weighted average estimated fair value of options at original grant date | $12.47 | $11.50 | $11.15 |

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The share-based compensation expense on awards held by employees of Temple-Inland will be based on the original grant date Black-Scholes-Merton value. The expected stock price volatility is based on historical prices of our common stock for a period corresponding to the expected life of the options with appropriate consideration given to current conditions and events. The expected life of options is based on historical experience. We use historical data to estimate pre-vesting forfeitures stratified into two groups based on job level.

**Share-based compensation expense**

Share-based compensation expense consists of:

| | For the Year | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| | (In millions) | | |
| Restricted or performance units-cash | $23 | $15 | $ 3 |
| Restricted or performance units-stock | 6 | 11 | 13 |
| Stock options | 10 | 12 | 5 |
| 401(k) match | — | — | 5 |
| | $39 | $38 | $26 |

Share-based compensation expense is included in:

| | For the Year | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| | (In millions) | | |
| Cost of sales | $ 7 | $ 6 | $ 5 |
| Selling expense | 2 | 1 | 1 |
| General and administrative | 25 | 31 | 20 |
| Other operating income (expense) | 5 | — | — |
| | $39 | $38 | $26 |

Share-based compensation expense for awards granted to Forestar and Guaranty employees is included in discontinued operations.

The amount of share-based compensation capitalized was not significant. We contributed treasury stock to fulfill our 401(k) matching obligation in first quarter 2005.

The fair value of awards granted to retirement-eligible employees and expensed at the date of grant was $3 million in 2007, primarily related to stock options. The increase in share-based compensation in 2006 is due to an increase in our share price.

Unrecognized share-based compensation for all awards not vested was $23 million at year-end 2007. It is likely that this cost will be recognized as expense over the next 3 years.

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## Note 10 — Other Operating Income (Expense)

| | For the Year | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| | (In millions) | | |
| Transformation costs | $ (69) | $— | $ — |
| Closures and sales of converting and production facilities and sales of non-strategic assets | (55) | (4) | (50) |
| Litigation | (56) | (6) | (13) |
| Environmental remediation | (9) | (8) | (3) |
| Softwood Lumber Agreement | — | 42 | — |
| Hurricane related costs, and in 2006, related insurance recoveries | — | 2 | (16) |
| Other charges | (5) | (5) | (3) |
| Equity in earnings of manufacturing joint ventures | 5 | 11 | 39 |
| | $(189) | $32 | $(46) |

We continue our efforts to enhance return on investment by lowering costs, improving operating efficiencies, and increasing asset utilization. As a result, we continue to review operations that are unable to meet return objectives and determine appropriate courses of action, including consolidating and closing facilities and selling under-performing assets.

In 2007, we permanently ceased production at our Mt. Jewett particleboard manufacturing facility, which we lease from a third party. As a result, we recognized charges of $64 million, including $60 million that represents the present value of the $77 million of future operating lease payments. This charge does not affect our continuing obligations under the lease, including paying rent and maintaining the equipment. The present value of the future payments is included on our balance sheet, of which $3 million is included in current liabilities and $57 million in other long-term liabilities.

In December 2007, we entered into arbitration in an effort to resolve most of the remaining claims regarding an alleged violation of Section 1 of the Sherman Act. The arbitrator awarded plaintiffs $46 million on the claims submitted to arbitration. Also in 2007, we reached agreements to settle three of the five cases in California state court alleging violations of that state's on duty meal break laws. We recognized $10 million of litigation expense in 2007 related to this matter.

In 2006, we sold one corrugated packaging converting facility, sold certain non-strategic assets, and finalized our estimates of losses related to the prior year's closures. In addition, we increased accruals for ongoing environmental remediation at the Antioch, California paper mill site closed in connection with our acquisition of Gaylord in 2002. As a result of these actions, we recognized losses of $12 million. Also in 2006, we received $42 million in connection with the Softwood Lumber Agreement between the U.S. and Canada, and we received $2 million of insurance proceeds related to cost incurred in connection with the 2005 hurricanes.

In 2005, we closed four corrugated packaging facilities, sold our Pembroke, Canada MDF facility, and effected other workforce reductions. As a result, we recognized losses of $53 million, including $38 million in impairments and losses on sales, $8 million in severance and retention obligations, and $7 million in other exit costs. The loss on the sale of the Pembroke MDF facility was $25 million, and other exit costs associated with the sale were $1 million. Also in 2005, Hurricanes Katrina and Rita adversely affected our operations. In addition to being forced to curtail production and incur start up costs at several facilities, we recognized losses and unusual expenses of $16 million, including $7 million in impairments related to our Texas and Louisiana timberland, $6 million in facility damages, and $3 million in employee and community assistance and other costs.

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Activity within our accruals for exit costs was:

| | Beginning of Year | Additions/ Revisions | Cash Payments | Year-End |
|---|---|---|---|---|
| | | (In millions) | | |
| For the Year 2007 | | | | |
| Involuntary employee terminations | $ 1 | $— | $ (1) | $— |
| Demolition and environmental remediation | 8 | 1(a) | (8) | 1 |
| | $ 9 | $ 1 | $ (9) | $ 1 |
| For the Year 2006 | | | | |
| Involuntary employee terminations | $ 1 | $ 1 | $ (1) | $ 1 |
| Contract termination penalties | 2 | — | (2) | — |
| Demolition and environmental remediation | 9 | 8(a) | (9) | 8 |
| | $12 | $ 9 | $(12) | $ 9 |
| For the Year 2005 | | | | |
| Involuntary employee terminations | $ 2 | $ 7 | $ (8) | $ 1 |
| Contract termination penalties | 6 | (4) | — | 2 |
| Demolition and environmental remediation | 16 | 1 | (8) | 9 |
| | $24 | $ 4 | $(16) | $12 |

(a) In 2007 and 2006, we revised our estimates relating to the demolition and related environmental remediation costs associated with our exit activities. We added $6 million in 2007 and $8 million in 2006 to this accrual by charging other operating expense. We transferred $6 million to Forestar as part of the spin-off.

## Note 11 — Income Taxes

Income tax expense on income from continuing operations consist of:

| | For the Year | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| | (In millions) | | |
| Current tax provision: | | | |
| U.S. Federal | $(278) | $ (57) | $ 57 |
| State and other | (10) | (8) | (3) |
| | (288) | (65) | 54 |
| Deferred tax provision: | | | |
| U.S. Federal | (410) | (43) | (47) |
| State and other | (55) | 5 | — |
| | (465) | (38) | (47) |
| Income tax expense | $(753) | $(103) | $ 7 |
| Income taxes (paid) refunded, net | $ 3 | $ (88) | $ 39 |

In 2007, we recognized one-time tax benefits of $3 million resulting from changes to the State of Texas margin tax enacted in May 2007 and another $4 million related to the settlement of state tax examinations.

In 2006, we entered into a settlement agreement with the U.S. Government to resolve pending tax litigation we filed to recover tax benefits promised to us in connection with our savings and loan acquisitions in 1988. Under the terms of the settlement agreement, we received a $95 million non-taxable cash payment

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for past and future tax benefits that would have been available to us had legislation enacted in 1993 not eliminated those tax benefits and $4 million of taxable interest income. In connection with the settlement, we incurred legal fees of $10 million, which were contingent upon the settlement. The net pre-tax gain related to this settlement was $89 million and is included in other non-operating income (expense).

Also in 2006, the Texas State Legislature enacted a new margin tax to replace the existing franchise tax, which for us results in a lower overall State of Texas tax rate. As a result, we recognized a one-time, non-cash benefit of $6 million of which $2 million related to the reduction of previously provided deferred state income taxes and $4 million related to reducing the valuation allowance for Texas investment credits.

In 2005, we recognized a one-time tax benefit of $16 million as a result of the sale of our Pembroke, Canada MDF facility.

Income from continuing operations before taxes consist of:

| | For the Year | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| | (In millions) | | |
| U.S. | $1,948 | $381 | $ 4 |
| Non-U.S. | 7 | 9 | 7 |
| | $1,955 | $390 | $11 |

A reconciliation of the federal statutory rate to the effective income tax rate on continuing operations follows:

| | For the Year | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| Federal statutory rate | 35% | 35% | 35% |
| State, net of federal benefit | 3 | — | 15 |
| Foreign | — | — | (4) |
| Other | 1 | — | 37 |
| | 39% | 35% | 83% |
| Settlement of tax litigation | — | (8) | — |
| State of Texas tax legislation | — | (1) | — |
| Sale of foreign subsidiary | — | — | (147) |
| Effective tax rate | 39% | 26% | (64)% |

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Significant components of deferred taxes are:

| | At Year-End | |
|---|---|---|
| | 2007 | 2006 |
| | (In millions) | |
| **Deferred Tax Liabilities:** | | |
| Property, equipment, and intangible assets | $(350) | $(330) |
| Timber and timberland, including deferred gain on sale in 2007 | (822) | (77) |
| U.S. taxes on unremitted foreign earnings | (16) | (14) |
| Other | (4) | (15) |
| | (1,192) | (436) |
| **Deferred Tax Assets:** | | |
| Alternative minimum tax credits | 286 | — |
| Foreign and state net operating loss carryforwards | 22 | 26 |
| Pension and postretirement benefits | 104 | 140 |
| Employee benefits | 59 | 53 |
| Accruals not deductible until paid | 51 | 31 |
| Other | 35 | 30 |
| Gross deferred tax assets | 557 | 280 |
| Less valuation allowance | (28) | (27) |
| | 529 | 253 |
| **Net Deferred Tax Liability** | $(663) | $(183) |

The net deferred tax liability is classified on our balance sheet as follows:

| | At Year-End | |
|---|---|---|
| | 2007 | 2006 |
| | (In millions) | |
| Current deferred tax assets | $ 99 | $ 61 |
| Non-current deferred tax liabilities | (762) | (244) |
| Net deferred tax liability | $(663) | $(183) |

The increase in deferred taxes primarily reflects the deferred gain on the sale of our strategic timberland offset by the resulting payment of alternative minimum taxes. Our alternative minimum tax credit can be carried forward indefinitely. Our foreign and state net operating loss carryforwards and credits will expire from 2008 through 2027. A valuation allowance is provided for these foreign and state net operating loss carryforwards and credits.

We or one of our subsidiaries files U.S. federal income tax returns, and income tax returns in various states and foreign jurisdictions. The Internal Revenue Service has completed the examinations of our tax returns through 2003, and we are no longer subject to examination by state or foreign tax authorities for years before 2000. We have various income tax audits in process as of year-end 2007, and we do not expect that the resolution of these matters will have a significant effect on our earnings or financial position.

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A reconciliation of the beginning and ending amount of unrecognized tax benefits is as follows:

| | (In millions) |
|---|---|
| Balance beginning of 2007 | $20 |
| Additions based on tax positions related to the current year | 4 |
| Reductions for tax positions of prior years | (1) |
| Settlements/collections | 3 |
| Balance end of 2007 | $26 |

Of the $26 million of unrecognized tax benefits, $13 million would affect our effective tax rate if recognized. Interest accrued related to unrecognized tax benefits is included in income tax (expense) benefit. Unrecognized tax benefits includes approximately $1 million of accrued interest and no penalties related to years 2007, 2006, and 2005. We do not expect material changes to our tax reserve during the next 12 months.

**Note 12 — Litigation**

We are involved in various legal proceedings that arise from time to time in the ordinary course of doing business and believe that adequate reserves have been established for any probable losses. Expenses related to litigation are included in operating income. We do not believe that the outcome of any of these proceedings should have a significant adverse effect on our financial position, long-term results of operations, or cash flows. It is possible, however, that charges related to these matters could be significant to our results or cash flows in any one accounting period.

We are a defendant in litigation alleging a civil violation of Section 1 of the Sherman Act. We and the other defendants have entered into various settlement agreements that resolved the class action portion of this litigation and the majority of the opt-out claims. Our payments under the settlement agreements have totaled $59 million of which $46 million was paid in 2007, $5 million in 2005, and $8 million in 2003. The trial for our one remaining state court claim is presently scheduled for first quarter 2008. We believe that we have established adequate reserves for this case.

We are also defending two cases in California state court alleging violations of that state's on duty meal break laws. In 2007, we settled three additional meal break cases. We believe we have established adequate reserves for these cases.

**Note 13 — Commitments and Other Contingencies**

We lease manufacturing and other facilities and equipment under operating lease agreements. Future minimum rental commitments under non-cancelable operating leases having a remaining term in excess of one year are (in millions): 2008 — $38; 2009 — $34; 2010 — $27; 2011 — $22; 2012 — $18; and thereafter — $83. Total rent expense was $43 million in 2007, $43 million in 2006, and $46 million in 2005. In 2007, we recorded an impairment charge related to a long-term operating lease. As a result, $60 million of our future operating lease payments are included on our balance sheet, of which $3 million is in current liabilities and $57 million is in other long-term liabilities.

We also lease two production facilities under sale-lease back transactions with two municipalities. The municipalities purchased the production facilities from us in 1992 and 1995 for $188 million, our carrying value, and we leased the facilities back from the municipalities under lease agreements, which expire in 2022 and 2025. Concurrently, we purchased $188 million of interest-bearing bonds issued by these municipalities. The bonds have terms that are identical to the lease terms, are secured by payments under the capital lease obligation, and the municipalities are obligated only to the extent the underlying lease payments are made by us. The interest rates implicit in the leases are the same as the interest rates on the bonds. As a result, the present value of the capital lease obligations is $188 million, the same as the principal amount of the bonds.

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Because there is no legal right of offset, the bonds are included in other assets at their cost of $188 million and the $188 million present value of the sale-lease back obligations are included in other long-term liabilities. The implicit interest expense on the leases and the interest income on the bonds are included in other non-operating income (expense). There is no net effect from these transactions as we are in substance both the obligor on, and the holder of, the bonds.

At year-end 2007, we had unconditional purchase obligations, principally for sawtimber, pulpwood and gypsum, aggregating $3.173 billion that will be paid over the next twelve to twenty years. This includes $1.470 billion related to a 20-year fiber supply agreement for pulpwood and a 12-year fiber supply agreement for sawtimber. Both of these agreements are subject to extension. These purchase obligations are valued at year-end 2007 market prices, however, our actual future purchases will be at the then current market price.

In connection with our joint venture operations, we have guaranteed debt service and other obligations and letters of credit aggregating $70 million at year-end 2007. Generally we would fund these guarantees for lack of specific performance by the joint ventures, such as non-payment of debt.

**Note 14 — Derivative Instruments and Variable Interest Entities**

We have used interest rate agreements in the normal course of business to mitigate the risk inherent in interest rate fluctuations by entering into contracts with major U.S. securities firms. At year-end 2007, we have two interest rate swap agreements that mature in 2008. The two agreements have a total notional amount of $50 million.

Under these swap agreements, we pay a fixed interest rate of 6.55 percent and receive a floating interest rate (4.60 percent at year-end 2007). At year-end 2007, the fair value of these interest rate swaps was a $1 million liability which is included in other current liabilities. The interest rate swap agreements were initially designated as a hedge of interest cash flows anticipated from specific variable-rate borrowings. By year-end 2007, no portion of the interest rate swap agreements qualified for hedge accounting since we have repaid virtually all of our variable-rate borrowings. Changes in the fair value of the interest rate swap agreements that qualified for hedge accounting increased other comprehensive income by $1 million in 2006 and decreased other comprehensive income $1 million in 2005. There was no material hedge ineffectiveness in 2006 or 2005. As a result of the termination of the hedge designation in 2007, we reclassified less than $1 million from other comprehensive income and charged other non-operating expense. Changes in the fair value of the interest rate swap agreements that did not qualify for hedge accounting were less than $1 million of expense in 2007, $1 million of income in 2006, and $2 million of income in 2005, and are included in other non-operating income (expense).

We also have used, to a limited degree, derivative instruments to mitigate our exposure to changes in anticipated cash flows from sale of products and manufacturing costs. These derivative contracts had notional amounts that represent less than one percent of our annual sales of linerboard and purchases of recycled fiber. These instruments expired in 2005. Operating income increased $1 million in 2005 as a result of linerboard and recycled fiber derivatives, and there was no material hedge ineffectiveness.

In 1999, we entered into an agreement to lease particleboard and medium density fiberboard facilities in Mt. Jewett, Pennsylvania. The lease is for 20 years and includes fixed price purchase options in 2014 and at the end of the lease. The option prices were intended to approximate the estimated fair values of the facilities at those dates and do not represent a guarantee of the facilities' residual values. After exhaustive efforts, we were unable to determine whether the lease is with a variable interest entity or if there is a primary beneficiary because the unrelated third-party lessors will not provide the necessary financial information. We account for the lease as an operating lease, and at year-end 2007 our financial interest was limited to our obligation to make the remaining $146 million of contractual lease payments, approximately $12 million per year.

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## Note 15 — Other Information

Our allowance for doubtful accounts was $14 million at year-end 2007 and $14 million at year-end 2006. The provision for doubtful accounts was $3 million in 2007, $3 million in 2006, and $4 million in 2005. Accounts charged-off, net of recoveries were $3 million in 2007, $3 million in 2006, and $6 million in 2005.

## Note 16 — Fair Value of Financial Instruments

Carrying value and the estimated fair value of our financial instruments are:

| | At Year-End | | | |
|---|---|---|---|---|
| | 2007 | | 2006 | |
| | Carrying Value | Fair Value | Carrying Value | Fair Value |
| | (In millions) | | | |
| **Financial liabilities** | | | | |
| Fixed-rate, long-term debt | $854 | $909 | $1,413 | $1,483 |

Differences between carrying value and fair value are primarily due to instruments that provide fixed interest rates or contain fixed interest rate elements. Inherently, such instruments are subject to fluctuations in fair value due to subsequent movements in interest rates. We value other financial instruments using quoted market prices where available or expected cash flows, discounted using rates that represent current rates for similar instruments. We excluded financial instruments from the table that are either carried at fair value or have fair values that approximate their carrying amount due to their short-term nature or variable interest rates.

At year-end 2007, we had guaranteed joint venture obligations principally related to fixed-rate debt instruments totaling $70 million. The estimated fair value of these guarantees is not significant.

## Note 17 — Earnings Per Share

We compute earnings per share by dividing income by weighted average shares outstanding using the following:

| | For the Year | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| | (In millions) | | |
| Earnings for basic and diluted earnings per share: | | | |
| Income from continuing operations | $1,202 | $ 287 | $ 18 |
| Discontinued operations | 103 | 181 | 158 |
| Net income | $1,305 | $ 468 | $ 176 |
| Weighted average shares outstanding: | | | |
| Weighted average shares outstanding — basic | 106.0 | 108.8 | 112.6 |
| Dilutive effect of equity purchase contracts | — | — | 0.4 |
| Dilutive effect of stock options (Note 9) | 2.1 | 2.0 | 1.5 |
| Weighted average shares outstanding — diluted | 108.1 | 110.8 | 114.5 |

Average common shares outstanding exclude unvested restricted shares. At year-end 2007, options for 1,122,545 shares were antidilutive.

Certain employees of Forestar and Guaranty participated in our employee stock option program. Following the spin-offs, these employees retained stock option rights associated with our stock. These stock options will remain a consideration in our dilutive effect of stock options until they are exercised, cancelled or expire. At year-end 2007, employees of Forestar and Guaranty held options for 1,236,437 shares of Temple-

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Inland stock, of which 551,627 were exercisable. The weighted average exercise price of these options at year-end 2007 was $17 per share and the weighted average remaining contractual term is 7 years.

## Note 18 — Segment Information

At year-end 2007, we have two business segments: corrugated packaging and building products. Timber and timberland is no longer an active segment as a result of the sale of our timberlands in fourth quarter 2007. Corrugated packaging manufactures containerboard and corrugated packaging. Building products manufactures a variety of building products. Timber and timberland managed our timber resources.

We evaluate performance based on operating income before unallocated items and income taxes. Unallocated items represent items managed on a company-wide basis and include corporate general and administrative expense, share-based compensation, other operating and non-operating income (expense), and interest expense. Other operating income (expense) includes gain or loss on sale of assets, asset impairments, and unusual expenses. The accounting policies of the segments are the same as those described in the accounting policy notes to the financial statements. Intersegment sales are recorded at market prices. Intersegment sales and shared service expense allocations are netted in costs and expenses.

| | Corrugated Packaging | Building Products | Timber and Timberland | Items Not Allocated to Segments and Eliminations | Total |
|---|---|---|---|---|---|
| | | | (In millions) | | |
| **For the year or at year-end 2007:** | | | | | |
| Revenues from external customers | $3,044 | $ 806 | $ 76 | $ — | $3,926 |
| Depreciation and amortization | 142 | 45 | 11 | 16 | 214 |
| Equity income from joint ventures | 4 | 1 | — | — | 5 |
| Income (loss) from continuing operations before taxes | 287 | 8 | 65 | 1,595[b] | 1,955 |
| Total assets | 2,301 | 623 | — | 3,018 | 5,942 |
| Investment in equity method investees and joint ventures | 11 | 23 | — | — | 34 |
| Goodwill | 236 | 129 | — | — | 365 |
| Capital expenditures and reforestation | 167 | 42 | 13 | 15 | 237 |
| **For the year or at year-end 2006:** | | | | | |
| Revenues from external customers | $2,977 | $1,119 | $ 89 | $ — | $4,185 |
| Depreciation and amortization | 153 | 44 | 14 | 14 | 225 |
| Equity income from joint ventures | 8 | 3 | — | — | 11 |
| Income (loss) from continuing operations before taxes | 255 | 221 | 63 | (149)[b] | 390 |
| Total assets | 2,275 | 638 | 330 | 384 | 3,627[a] |
| Investment in equity method investees and joint ventures | 11 | 22 | — | — | 33 |
| Goodwill | 236 | 129 | — | — | 365 |
| Capital expenditures and reforestation | 117 | 46 | 19 | 22 | 204 |
| **For the year or at year-end 2005:** | | | | | |
| Revenues from external customers | $2,825 | $ 898 | $120 | $ — | $3,843 |
| Depreciation and amortization | 160 | 35 | 12 | 11 | 218 |
| Equity income from joint ventures | 11 | 28 | — | — | 39 |
| Income (loss) from continuing operations before taxes | 120 | 125 | 72 | (306)[b] | 11 |
| Total assets | 2,308 | 456 | 333 | 314 | 3,411[a] |
| Investment in equity method investees and joint ventures | 11 | 36 | — | — | 47 |
| Goodwill | 236 | — | — | — | 236 |
| Capital expenditures and reforestation | 126 | 43 | 30 | 21 | 220 |

[a] Excludes assets of discontinued operations of $16,847 million in 2006 and $18,219 million in 2005.

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(b) Items not allocated to segments consists of:

| | For the Year | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| | (In millions) | | |
| General and administrative | $ (100) | $(107) | $ (91) |
| Share-based compensation | (34) | (38) | (21) |
| Gain on sale of timberland | 2,053 | — | — |
| Other operating income (expense) | (188) | 26 | (85) |
| Other non-operating income (expense) | (35) | 93 | — |
| Net interest income on financial assets and nonrecourse financial liabilities of special purpose entities | 10 | — | — |
| Interest | (111) | (123) | (109) |
| | $1,595 | $(149) | $(306) |
| Other operating income (expense) applies to: | | | |
| Corrugated packaging | $ (64) | $ (21) | $ (38) |
| Building products | (63) | 42 | (27) |
| Timber and timberland | 2,060 | — | — |
| Unallocated | (68) | 5 | (20) |
| | $1,865 | $ 26 | $ (85) |

Please read **Note 10** for further information about other operating income (expense).

Revenues and property and equipment based on the location of our operations were:

| Geographic Information | For the Year | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| | (In millions) | | |
| Revenues from external customers: | | | |
| United States | $3,739 | $4,009 | $3,660 |
| Mexico | 187 | 176 | 156 |
| Canada[a] | — | — | 27 |
| | $3,926 | $4,185 | $3,843 |

| | At Year-End | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| | (In millions) | | |
| Property and equipment: | | | |
| United States | $1,596 | $1,591 | $1,582 |
| Mexico | 36 | 37 | 38 |
| Canada[a] | — | — | 1 |
| | $1,632 | $1,628 | $1,621 |

(a) In 2005, we sold our MDF facility located in Pembroke, Canada, as a result, we have no significant assets or ongoing operations in Canada.

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## Note 19 — Summary of Quarterly Results of Operations (Unaudited)

Selected quarterly financial results for 2007 and 2006 have been reclassified to reflect Forestar and Guaranty as discontinued operations:

| | First Quarter | Second Quarter | Third Quarter | Fourth Quarter |
|---|---|---|---|---|
| | (In millions, except per share) | | | |
| **2007** | | | | |
| Total revenues | $1,003 | $1,023 | $ 963 | $ 937 |
| Gross profit | $ 144 | $ 146 | $ 129 | $ 117 |
| Income from continuing operations[(a)] | $ 7 | $ 26 | $ 11 | $1,158 |
| Discontinued operations | 31 | 40 | 25 | 7 |
| Net income | $ 38 | $ 66 | $ 36 | $1,165 |
| Earnings per share[(b)] | | | | |
| Basic: | | | | |
| Income from continuing operations | $ 0.07 | $ 0.24 | $0.11 | $10.88 |
| Discontinued operations | 0.29 | 0.39 | 0.23 | 0.08 |
| Net income | $ 0.36 | $ 0.63 | $0.34 | $10.96 |
| Diluted: | | | | |
| Income from continuing operations | $ 0.07 | $ 0.24 | $0.11 | $10.69 |
| Discontinued operations | 0.28 | 0.38 | 0.22 | 0.07 |
| Net income | $ 0.35 | $ 0.62 | $0.33 | $10.76 |

(a) Income from continuing operations includes the following items:

| | First Quarter | Second Quarter | Third Quarter | Fourth Quarter |
|---|---|---|---|---|
| | (In millions) | | | |
| Gain on sale of timberland | $ — | $— | $— | $2,053 |
| Other operating income (expense): | | | | |
| Transformation costs (advisory and legal fees, change of control and employee related) | $ (4) | $(4) | $(2) | $ (59) |
| Closures and sales of converting and production facilities and sales of non-strategic assets | — | 8 | (1) | (62) |
| Litigation | (10) | — | — | (46) |
| Environmental remediation | — | — | — | (9) |
| Other | — | (5) | (3) | 9 |
| | $(14) | $(1) | $(6) | $ (167) |
| Other non-operating income (expense): | | | | |
| Charges related to early repayment of debt | $ — | $— | $— | $ (40) |
| Interest and other income | — | 1 | 1 | 3 |
| | $ — | $ 1 | $ 1 | $ (37) |

(b) The sum of earnings per share for the quarters does not equal earnings per share for the year due to the use of average shares outstanding for each period.

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| | First Quarter | Second Quarter | Third Quarter | Fourth Quarter |
|---|---|---|---|---|
| | (In millions, except per share) | | | |
| **2006** | | | | |
| Total revenues | $1,043 | $1,090 | $1,051 | $1,001 |
| Gross profit | $ 155 | $ 203 | $ 190 | $ 161 |
| Income from continuing operations[a][b] | $ 29 | $ 148 | $ 49 | $ 61 |
| Discontinued operations | 50 | 43 | 46 | 42 |
| Net income[b] | $ 79 | $ 191 | $ 95 | $ 103 |
| Earnings per share[c] | | | | |
| Basic: | | | | |
| Income from continuing operations[b] | $ 0.26 | $ 1.35 | $ 0.45 | $ 0.59 |
| Discontinued operations | 0.45 | 0.39 | 0.42 | 0.40 |
| Net income[b] | $ 0.71 | $ 1.74 | $ 0.87 | $ 0.99 |
| Diluted: | | | | |
| Income from continuing operations[b] | $ 0.26 | $ 1.32 | $ 0.44 | $ 0.57 |
| Discontinued operations | 0.44 | 0.38 | 0.42 | 0.39 |
| Net income[b] | $ 0.70 | $ 1.70 | $ 0.86 | $ 0.96 |

(a) Income from continuing operations includes the following items:

| | First Quarter | Second Quarter | Third Quarter | Fourth Quarter |
|---|---|---|---|---|
| | (In millions) | | | |
| Other operating income (expense): | | | | |
| Closures and sales of converting and production facilities and sales of non-strategic assets | $— | $(1) | $(4) | $ 1 |
| Litigation | — | — | (4) | (2) |
| Environmental remediation | — | — | — | (8) |
| Softwood Lumber Agreement | — | — | — | 42 |
| Hurricane related insurance recoveries | — | — | — | 2 |
| | $— | $(1) | $(8) | $35 |
| Other non-operating income (expense): | | | | |
| Tax litigation settlement | $— | $89 | $— | $— |
| Interest and other income | 1 | 2 | 1 | — |
| | $ 1 | $91 | $ 1 | $— |

(b) 2006 quarters have been recast for the retrospective application of FASB Staff Position No. AUG AIR — 1 *Accounting for Planned Major Maintenance.*

(c) The sum of earnings per share for the quarters does not equal earnings per share for the year due to the use of average shares outstanding for each period.

## Note 20 — Discontinued Operations

On December 28, 2007, we spun off to our shareholders in tax-free distributions, our real estate segment and our financial services segment, which included certain real estate and minerals activities in our timber and timberland segment.

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As a result, we report the assets and liabilities and results of operations of these segments as discontinued operations. Expense allocated to these discontinued operations included interest expense of $7 million in 2007, $4 million in 2006, and none in 2005 and share-based compensation expense of $7 million in 2007, $8 million in 2006, and $5 million in 2005.

In addition, on August 31, 2007 we sold the previously acquired chemical operations. We received cash proceeds of $1 million and recognized a pre-tax loss of $6 million on the sale. Assets of this operation were previously reported as assets held-for-sale. We have ongoing environmental remediation activities related to this operation for which we have established a reserve. Any changes to our estimate of cost will impact current operations.

A summary of the assets and liabilities of discontinued operations at year-end 2006 follows:

| | Real Estate | Financial Services | Chemical Operations and Other | Total |
|---|---|---|---|---|
| | | (In millions) | | |
| Cash and cash equivalents | $ 3 | $ 372 | $ 5 | $ 380 |
| Loans and loans held for sale | — | 9,640 | — | 9,640 |
| Securities | — | 5,644 | — | 5,644 |
| Real estate | 564 | — | — | 564 |
| Property and equipment | 2 | 214 | 7 | 223 |
| Other assets | 31 | 357 | 8 | 396 |
| Total Assets | $600 | $16,227 | $20 | $16,847 |
| Deposits | $ — | $ 9,486 | $— | $ 9,486 |
| Debt | 44 | 5,177 | — | 5,221 |
| Other liabilities | 43 | 87 | 7 | 137 |
| Subordinated notes payable to trust | — | 142 | — | 142 |
| Preferred stock issued by subsidiaries | — | 305 | — | 305 |
| Total Liabilities | $ 87 | $15,197 | $ 7 | $15,291 |

A summary of earnings from our discontinued operations follows:

| | For the Year | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| | (In millions) | | |
| Real estate income before taxes | $ 41 | $ 83 | $ 59 |
| Financial services income before taxes | 138 | 204 | 192 |
| Chemical operations and other[(a)] | (13) | (2) | 1 |
| Income from discontinued operations before taxes | 166 | 285 | 252 |
| Income tax expense | (63) | (104) | (94) |
| Discontinued operations | $103 | $ 181 | $158 |

(a) 2007 includes a $6 million charge for environmental remediation.

## Note 21 — Subsequent Events

On February 1, 2008, our Board of Directors declared a quarterly dividend of $0.10 per share payable on March 14, 2008.

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**Item 9.** ***Changes in and Disagreements with Accountants on Accounting and Financial Disclosure***

We have had no changes in or disagreements with our independent registered public accounting firm to report.

**Item 9A.** ***Controls and Procedures***

(a) Disclosure controls and procedures

Our management, with the participation of the Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (or the Exchange Act)) as of the end of the period covered by this report. Based on such evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that, as of the end of such period, our disclosure controls and procedures are effective in recording, processing, summarizing and reporting, on a timely basis, information required to be disclosed by us in the reports that we file or submit under the Exchange Act and are effective in ensuring that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

(b) Internal control over financial reporting

Management's report on internal control over financial reporting is included in **Item 8. Financial Statements and Supplementary Data.**

There have not been any changes in our internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) in fourth quarter 2007 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

**Item 9B.** ***Other Information***

None.

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## PART III

### Item 10. *Directors, Executive Officers and Corporate Governance*

Set forth below is certain information about the members of our Board of Directors:

| Name | Age | Year First Elected to the Board | Principal Occupation |
|---|---|---|---|
| Doyle R. Simons | 44 | 2007 | Chairman and Chief Executive Officer of Temple-Inland Inc. |
| Afsaneh M. Beschloss | 52 | 2002 | President and Chief Executive Officer of The Rock Creek Group |
| Dr. Donald M. Carlton | 70 | 2003 | Former President and Chief Executive Officer of Radian International LLC |
| Cassandra C. Carr | 63 | 2004 | Senior Advisor, Public Strategies, Inc. |
| E. Linn Draper, Jr. | 66 | 2004 | Former Chairman, President and Chief Executive Officer of American Electric Power Company, Inc. |
| Larry R. Faulkner | 62 | 2005 | President of Houston Endowment Inc. |
| James T. Hackett | 54 | 2000 | Chairman, President and Chief Executive Officer of Anadarko Petroleum Corporation |
| Jeffrey M. Heller | 68 | 2004 | Vice Chairman of Electronic Data Systems, Inc. |
| J. Patrick Maley, III | 46 | 2007 | President and Chief Operating Officer of Temple-Inland Inc. |
| W. Allen Reed | 60 | 2000 | Former Chairman of the Board of General Motors Asset Management Corporation |
| Richard M. Smith | 62 | 2006 | Chairman of Newsweek |
| Arthur Temple III | 66 | 1983 | Chairman of the Board of First Bank & Trust, East Texas and the T.L.L. Temple Foundation |
| Larry E. Temple | 72 | 1991 | Attorney-at-law |

The remaining information required by this item is incorporated herein by reference from our definitive proxy statement, involving the election of directors, to be filed pursuant to Regulation 14A with the SEC not later than 120 days after the end of the fiscal year covered by this Form 10-K (or Definitive Proxy Statement). Certain information required by this item concerning executive officers is included in Part I of this report.

### Item 11. *Executive Compensation*

The information required by this item is incorporated by reference from our Definitive Proxy Statement.

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**Item 12.** ***Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters***

**Securities Authorized for Issuance Under Equity Compensation Plans**

Information at year-end 2007 about our compensation plans under which our Common Stock may be issued follows:

| Plan Category | (a) Number of Securities to be Issued Upon Exercise of Outstanding Options, Warrants and Rights | (b) Weighted-Average Exercise Price of Outstanding Options, Warrants and Rights | (c) Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans (Excluding Securities Reflected in Column(a)) |
|---|---|---|---|
| Equity compensation plans approved by security holders | 7,108,174 | $15 | None |
| Equity compensation plans not approved by security holders | None | None | None |
| Total | 7,108,174 | $15 | None |

The remaining information required by this item is incorporated by reference from our Definitive Proxy Statement.

**Item 13.** ***Certain Relationships and Related Transactions, and Director Independence***

The information required by this item is incorporated by reference from our Definitive Proxy Statement.

**Item 14.** ***Principal Accounting Fees and Services***

The information required by this item is incorporated by reference from our Definitive Proxy Statement.

## PART IV

**Item 15.** ***Exhibits, Financial Statement Schedules***

(a) Documents Filed as Part of Report.

1. *Financial Statements*

Our consolidated financial statements are included in Part II, Item 8 of this Annual Report on Form 10-K.

2. *Financial Statement Schedules*

All schedules are omitted as the required information is either inapplicable or the information is presented in our consolidated financial statements and notes thereto in Item 8 above.

3. *Exhibits*

| Exhibit Number | Exhibit |
|---|---|
| 3.01 | — Amended and Restated Certificate of Incorporation of the Company (incorporated by reference to Exhibit 3.1 to the Company's Form 10-Q for the quarter ended June 30, 2007, and filed with the Commission on August 7, 2007) |
| 3.02 | — Amended and Restated Bylaws of the Company (incorporated by reference to Exhibit 3.2 to the Company's Form 10-Q for the quarter ended June 30, 2007, and filed with the Commission on August 7, 2007) |
| 4.01 | — Form of Specimen Common Stock Certificate of the Company (incorporated by reference to Exhibit 4.03 to registration statement on Form S-8 (Reg. No. 33-27286) filed by the Company with the Commission on March 2, 1989) |
| 4.02 | — Indenture dated as of September 1, 1986, between the Registrant and Bank of New York Trust Company, N.A. (successor to Chemical Bank), as Trustee (or Senior Notes Indenture) (incorporated by reference to Exhibit 4.01 to registration statement on Form S-1 (Reg. No. 33-8362) filed by the Company with the Commission on August 29, 1986) |

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| Exhibit Number | Exhibit |
|---|---|
| 4.03 | — First Supplemental Indenture to the Senior Notes Indenture, dated as of April 15, 1988, between the Company and Bank of New York Trust Company, N.A. (successor to The Chase Manhattan Bank and Chemical Bank), as Trustee (incorporated by reference to Exhibit 4.02 to registration statement on Form S-3, Registration No. 33-20431, filed with the Commission on March 2, 1988) |
| 4.04 | — Second Supplemental Indenture to the Senior Notes Indenture, dated as of December 27, 1990, between the Company and Bank of New York Trust Company, N.A. (successor to The Chase Manhattan Bank and Chemical Bank), as Trustee (incorporated by reference to Exhibit 4.03 to Form 8-K, filed with the Commission on December 27, 1990) |
| 4.05 | — Third Supplemental Indenture to the Senior Notes Indenture, dated as of May 9, 1991, between the Company and Bank of New York Trust Company, N.A. (successor to The Chase Manhattan Bank and Chemical Bank), as Trustee (incorporated by reference to Exhibit 4 to Form 10-Q for the quarter ended June 29, 1991, filed with the Commission on August 7, 1991) |
| 4.06 | — Certificate of Designation, Preferences and Rights of Series A Junior Participating Preferred Stock, dated February 16, 1989 (incorporated by reference to Exhibit 4.04 to the Company's Form 10-K for the year ended December 31, 1988, and filed with the Commission on March 21, 1989) |
| 4.07 | — Rights Agreement, dated February 20, 1999, between the Company and Computershare Trust Company, N.A. (f/k/a First Chicago Trust Company of New York), as Rights Agent (incorporated by reference to Exhibit 1 to the Company's registration statement on Form 8A filed with the Commission on February 19, 1999) |
| 4.08 | — Form of Fixed-rate Medium Term Note, Series F, of the Company (incorporated by reference to Exhibit 4.05 to the Company's Form 8-K filed with the Commission on June 3, 1998) |
| 4.09 | — Form of 7.875% Senior Notes due 2012 of the Company (incorporated by reference to Exhibit 4.1 to the Company's Form 8-K filed with the Commission on May 3, 2002) |
| 4.10 | — Form of 6.375% Senior Notes due 2016 of the Company (incorporated by reference to Exhibit 4.1 to the Company's Form 8-K filed with the Commission on December 6, 2005) |
| 4.11 | — Form of 6.625% Senior Notes due 2018 of the Company (incorporated by reference to Exhibit 4.2 to the Company's Form 8-K filed with the Commission on December 6, 2005) |
| 10.01 | — Credit Agreement dated July 28, 2005, with Bank of America, N.A., as administrative agent and L/C Issuer; Citibank, N.A. and The Toronto Dominion Bank, as co-syndication agents; BNP Paribas and The Bank Of Nova Scotia, as co-documentation agents; Banc of America Securities LLC and Citigroup Global Markets Inc., as joint lead arrangers and joint book managers; and the lenders party thereto (incorporated by reference to the Company's Current Report on Form 8-K filed with the Commission on August 1, 2005) |
| 10.02* | — Temple-Inland Inc. 1993 Stock Option Plan (incorporated by reference to the Company's definitive proxy statement in connection with the Annual Meeting of Shareholders held May 6, 1994, and filed with the Commission on March 21, 1994) |
| 10.03* | — First amendment to Temple-Inland Inc. 1993 Stock Option Plan (incorporated by reference to Exhibit 10.1 to the Company's Form 10-Q for the quarter ended September 30, 2006, and filed with the Commission on November 7, 2006) |
| 10.04* | — Temple-Inland Inc. 1997 Stock Option Plan (incorporated by reference to the Company's Definitive Proxy Statement in connection with the Annual Meeting of Shareholders held May 2, 1997, and filed with the Commission on March 17, 1997), as amended May 7, 1999 (incorporated by reference to the Company's definitive proxy statement in connection with the Annual Meeting of Shareholders held May 7, 1999, and filed with the Commission on March 26, 1999) |
| 10.05* | — First amendment to Temple-Inland Inc. 1997 Stock Option Plan (incorporated by reference to Exhibit 10.2 to the Company's Form 10-Q for the quarter ended September 30, 2006, and filed with the Commission on November 7, 2006) |
| 10.06* | — Temple-Inland Inc. 1997 Restricted Stock Plan (incorporated by reference to the Company's Definitive Proxy Statement in connection with the Annual Meeting of Shareholders held May 2, 1997, and filed with the Commission on March 17, 1997) |
| 10.07* | — Temple-Inland Inc. 2001 Stock Incentive Plan (incorporated by reference to the Company's definitive proxy statement in connection with the Annual Meeting of Shareholders held May 4, 2001, and filed with the Commission on March 23, 2001) |

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| Exhibit Number | Exhibit |
|---|---|
| 10.08* | — First amendment to Temple-Inland Inc. 2001 Stock Incentive Plan (incorporated by reference to Exhibit 10.3 to the Company's Form 10-Q for the quarter ended September 30, 2006, and filed with the Commission on November 7, 2006) |
| 10.09* | — Temple-Inland Inc. 2003 Stock Incentive Plan (incorporated by reference to Appendix A of the Company's definitive proxy statement dated March 31, 2003, and prepared in connection with the annual meeting of stockholders held May 2, 2003) |
| 10.10* | — First amendment to Temple-Inland Inc. 2003 Stock Incentive Plan (incorporated by reference to Exhibit 10.4 to the Company's Form 10-Q for the quarter ended September 30, 2006, and filed with the Commission on November 7, 2006) |
| 10.11* | — Form of Nonqualified Stock Option Agreement issued pursuant to the Temple-Inland Inc. 2003 Stock Incentive Plan (incorporated by reference to Exhibit 10.23 to the Company's Form 10-K for the year ended January 3, 2004, and filed with the Commission on February 23, 2004) |
| 10.12* | — Revised Form of Performance Stock Units Agreement issued pursuant to the Temple-Inland Inc. 2003 Stock Incentive Plan (incorporated by reference to Exhibit 10.08 to the Company's Form 10-K for the year ended December 31, 2005, and filed with the commission on March 8, 2006) |
| 10.13* | — Revised Form of Restricted Stock Unit Agreement issued pursuant to the Temple-Inland Inc. 2003 Stock Incentive Plan (incorporated by reference to Exhibit 10.09 to the Company's Form 10-K for the year ended December 31, 2005, and filed with the commission on March 8, 2006) |
| 10.14* | — Revised Form of Nonqualified Stock Option Agreement for Non-Employee Directors issued pursuant to the Temple-Inland Inc. 2003 Stock Incentive Plan (incorporated by reference to Exhibit 10.10 to the Company's Form 10-K for the year ended December 31, 2005, and filed with the commission on March 8, 2006) |
| 10.15* | — Amendment to outstanding Temple-Inland Option Agreements and Restricted Stock Agreements (incorporated by reference to Exhibit 10.4 to the Company's Current Report on Form 8-K filed with the Commission on December 31, 2007) |
| 10.16* | — Amended and restated Temple-Inland Nonqualified Deferred Compensation Plan (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K filed with the Commission on December 31, 2007) |
| 10.17* | — Amended and restated Temple-Inland Directors' Fee Deferral Plan (incorporated by reference to Exhibit 10.2 to the Company's Current Report on Form 8-K filed with the Commission on December 31, 2007) |
| 10.18* | — Amended and restated Temple-Inland Supplemental Executive Retirement Plan (incorporated by reference to Exhibit 10.3 to the Company's Current Report on Form 8-K filed with the Commission on December 31, 2007) |
| 10.19* | — Employment Agreement between the company and Doyle R. Simons, dated August 9, 2007 (incorporated by reference to Exhibit 10.2 to the Company's Current Report on Form 8-K filed with the Commission on August 10, 2007) |
| 10.20* | — Change in Control Agreement dated June 1, 2003, between the Company and J. Patrick Maley III (incorporated by reference to Exhibit 10.1 to the Company's Form 10-Q for the quarter ended September 28, 2003, and filed with the Commission on November 12, 2003) |
| 10.21* | — Change in Control Agreement dated October 2, 2000, between the Company and Jack C. Sweeny (incorporated by reference to Exhibit 10.29 to the Company's Form 10-K for the year ended December 30, 2000, and filed with the Commission on March 5, 2001) |
| 10.22* | — Change in Control Agreement dated October 2, 2000, between the Company and Randall D. Levy (incorporated by reference to Exhibit 10.31 to the Company's Form 10-K for the year ended December 30, 2000, and filed with the Commission on March 5, 2001) |
| 10.23 | — Loan Agreement, dated December 3, 2007, by and among TIN Land Financing, LLC, Citibank, N.A., Citicorp North America, Inc., as Agent, and the other Lenders named therein (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K filed with the Commission on December 4, 2007) |
| 10.24 | — Loan Agreement, dated December 3, 2007, by and among TIN Timber Financing, LLC, Citibank, N.A., Citicorp North America, Inc., as Agent, and the other Lenders named therein (incorporated by reference to Exhibit 10.2 to the Company's Current Report on Form 8-K filed with the Commission on December 4, 2007) |
| 10.25 | — Pulpwood Supply Agreement, dated October 31, 2007, by and between TIN Inc. and CPT LOGCO, LLC (1)(2) |
| 10.26 | — Sawtimber Supply Agreement, dated October 31, 2007, by and between TIN Inc. and CPT LOGCO, LLC (1)(2) |
| 10.27* | — Temple-Inland Inc. 2008 Incentive Plan (1) (3) |

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| Exhibit Number | Exhibit |
|---|---|
| 10.28* | — Form of Nonqualified Stock Option Agreement, as revised in 2008, issued pursuant to the Temple-Inland Inc. 2003 Stock Incentive Plan (1) |
| 10.29* | — Form of Restricted Stock Units Agreement issued pursuant to the Temple-Inland Inc. 2008 Incentive Plan (1) |
| 21 | — Subsidiaries of the Company (1) |
| 23 | — Consent of Ernst & Young LLP (1) |
| 31.1 | — Certification of Chief Executive Officer pursuant to Exchange Act rule 13a-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (1) |
| 31.2 | — Certification of Chief Financial Officer pursuant to Exchange Act rule 13a-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (1) |
| 32.1 | — Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (1) |
| 32.2 | — Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (1) |

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* Management contract or compensatory plan or arrangement.

(1) Filed herewith

(2) Portions of this exhibit have been omitted pursuant to a request for confidential treatment filed with the Securities and Exchange Commission. The omissions have been indicated with asterisks ("***"), and the omitted text has been filed separately with the Commission.

(3) To be submitted for shareholder approval at the 2008 Annual Meeting of Stockholders.

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## SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, as amended, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

TEMPLE-INLAND INC.
(Registrant)

By: /s/ DOYLE R. SIMONS
Doyle R. Simons
*Chairman of the Board and*
*Chief Executive Officer*

Date: February 25, 2008

Pursuant to the requirements of the Securities Exchange Act of 1934, as amended, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

| Signature | Capacity | Date |
|---|---|---|
| /s/ DOYLE R. SIMONS<br>Doyle R. Simons | Director, Chairman of the Board, and Chief Executive Officer | February 25, 2008 |
| /s/ RANDALL D. LEVY<br>Randall D. Levy | Chief Financial Officer | February 25, 2008 |
| /s/ TROY L. HESTER<br>Troy L. Hester | Principal Accounting Officer | February 25, 2008 |
| /s/ AFSANEH M. BESCHLOSS<br>Afsaneh M. Beschloss | Director | February 25, 2008 |
| /s/ DONALD M. CARLTON<br>Donald M. Carlton | Director | February 25, 2008 |
| /s/ CASSANDRA C. CARR<br>Cassandra C. Carr | Director | February 25, 2008 |
| /s/ E. LINN DRAPER, JR.<br>E. Linn Draper, Jr. | Director | February 25, 2008 |
| /s/ LARRY R. FAULKNER<br>Larry R. Faulkner | Director | February 25, 2008 |
| /s/ JAMES T. HACKETT<br>James T. Hackett | Director | February 25, 2008 |
| /s/ JEFFREY M. HELLER<br>Jeffrey M. Heller | Director | February 25, 2008 |

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| Signature | Capacity | Date |
|---|---|---|
| /s/ J. Patrick Maley III<br>J. Patrick Maley III | Director | February 25, 2008 |
| /s/ W. Allen Reed<br>W. Allen Reed | Director | February 25, 2008 |
| /s/ Richard M. Smith<br>Richard M. Smith | Director | February 25, 2008 |
| /s/ Arthur Temple III<br>Arthur Temple III | Director | February 25, 2008 |
| /s/ Larry E. Temple<br>Larry E. Temple | Director | February 25, 2008 |

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**Exhibit 31.1**

## CERTIFICATION OF CHIEF EXECUTIVE OFFICER PURSUANT TO EXCHANGE ACT RULE 13a-14(a)

I, Doyle R. Simons, certify that:

1. I have reviewed this Annual Report on Form 10-K of Temple-Inland Inc.:

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)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) 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) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

c) 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

d) 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 (the registrant's fourth fiscal quarter in the case of an annual report) 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 registrant's 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.

/s/ Doyle R. Simons

Doyle R. Simons
Chief Executive Officer

Date: February 25, 2008

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**Exhibit 31.2**

## CERTIFICATION OF CHIEF FINANCIAL OFFICER PURSUANT TO EXCHANGE ACT RULE 13a-14(a)

I, Randall D. Levy, certify that:

1. I have reviewed this Annual Report on Form 10-K of Temple-Inland Inc.:

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)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) 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) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

c) 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

d) 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 (the registrant's fourth fiscal quarter in the case of an annual report) 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 registrant's 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.

/s/ Randall D. Levy

Randall D. Levy
Chief Financial Officer

Date: February 25, 2008

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# Temple-Inland Shareholder Information

### TRANSFER AGENT AND REGISTRAR
Computershare Trust Company, N.A.
250 Royall Street
Canton, MA 02021
781.575.2879

### INDEPENDENT AUDITORS
Ernst & Young LLP
Austin, Texas

### ANNUAL MEETING
The annual meeting of shareholders of Temple-Inland will be held at 303 South Temple Drive, Diboll, Texas, on Friday, May 2, 2008, at 9:00 a.m. CDT.

### STOCK LISTING
Temple-Inland's common stock is listed on the New York Stock Exchange under the ticker symbol TIN.

As of December 29, 2007, there were 4,786 shareholders of record of the Company's common stock.

### CEO ANNUAL CERTIFICATION TO THE NYSE
As required by the rules of the NYSE, on May 7, 2007, Kenneth M. Jastrow II, Chairman and CEO of Temple-Inland, filed a written affirmation with the NYSE certifying that he was not aware of any violation by the Company of any of the corporate governance listing standards of the NYSE.

### DIVIDEND REINVESTMENT PLAN
Temple-Inland offers its shareholders a convenient and economical way to increase their investment in the Company's common stock through the purchase of additional shares with quarterly dividends and optional cash payments. Under the Temple-Inland Dividend Reinvestment Plan, administered by Computershare Trust Company, N.A., Temple-Inland pays the brokerage fees and service charges, and the shareholder receives the benefit of larger quantity purchases and optional free custodial services. For more information about the plan, contact Computershare Trust Company, N.A., Dividend Reinvestment Plans, 250 Royall Street, Canton, MA 02021, 781.575.2879.

### COMPANY WEB SITE
Additional information regarding Temple-Inland, including the annual report on Form 10-K and other periodic reports filed with the Securities and Exchange Commission, may be obtained from Temple-Inland's home page on the Internet, the address of which is http://www.templeinland.com.

### MAILING ADDRESS
Temple-Inland Inc.
P.O. Box 40
Austin, Texas 78767
512.434.5800

**Temple-Inland Inc.**
**2007 Board Members**

**Afsaneh M. Beschloss**
President and Chief Executive Officer of The Rock Creek Group

**Donald M. Carlton**
Former President and Chief Executive Officer of Radian International LLC

**Cassandra C. Carr**
Senior Advisor, Public Strategies, Inc.

**E. Linn Draper, Jr.**
Former Chairman, President and Chief Executive Officer of American Electric Power Company, Inc.

**Larry R. Faulkner**
President of Houston Endowment, Inc.

**James T. Hackett**
Chairman, President and Chief Executive Officer of Anadarko Petroleum Corporation

**Jeffrey M. Heller**
Vice Chairman of Electronic Data Systems, Inc.

**J. Patrick Maley III**
President and Chief Operating Officer of Temple-Inland Inc.

**W. Allen Reed**
Former Chairman of General Motors Asset Management Corporation

**Doyle R. Simons**
Chairman and Chief Executive Officer of Temple-Inland Inc.

**Richard M. Smith**
Chairman of Newsweek

**Arthur Temple III**
Chairman of the Board of First Bank & Trust, East Texas and T.L.L. Temple Foundation

**Larry E. Temple**
Attorney-at-law

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