

ATLANTIS PLASTICS INC

Form 10-Q

November 19, 2007

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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549  
FORM 10-Q**

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

For the quarterly period ended September 30, 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 1-9487  
ATLANTIS PLASTICS, INC.**

(Exact name of registrant as specified in its charter)

DELAWARE

06-1088270

(State or other jurisdiction of incorporation or organization)

(IRS Employer Identification No.)

1870 The Exchange, Suite 200, Atlanta, Georgia

30339

(Address of principal executive offices)

(Zip Code)

(Registrant's telephone number, including Area Code) (800) 497-7659

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

Large Accelerated Filer  Accelerated Filer  Non-Accelerated Filer

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

Indicate the number of shares outstanding of each of the issuer's classes of Common Stock, as of the latest practicable date.

Class	Outstanding at September 30, 2007
Class A Common Stock, \$.0001 par value	6,141,009
Class B Common Stock, \$.0001 par value	2,114,814

**ATLANTIS PLASTICS, INC.**  
**FORM 10-Q**  
**For the Quarter Ended September 30, 2007**  
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**ATLANTIS PLASTICS, INC.**  
**CONSOLIDATED STATEMENTS OF LOSS**

<i>(In thousands, except per share data) (Unaudited)</i>	<b>Three Months Ended September 30,</b>		<b>Nine Months Ended September 30,</b>	
	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
Net sales	\$ 103,544	\$ 108,261	\$ 308,414	\$ 328,648
Cost of sales	93,505	97,120	272,961	289,646
Gross profit	10,039	11,141	35,453	39,002
Selling, general and administrative expenses	8,195	8,171	25,142	25,022
Goodwill impairment charge	12,854		12,854	
Severance and restructuring expenses	35	655	1,119	952
Operating (loss) income	(11,045)	2,315	(3,662)	13,028
Net interest expense	(7,087)	(5,083)	(18,679)	(14,655)
Other income (expense)	74	(17)	152	96
Loss before benefit for income taxes	(18,058)	(2,785)	(22,189)	(1,531)
Benefit for income taxes	(4,149)	(1,031)	(5,591)	(567)
<b>Net loss</b>	<b>\$ (13,909)</b>	<b>\$ (1,754)</b>	<b>\$ (16,598)</b>	<b>\$ (964)</b>
Loss per share Basic	\$ (1.68)	\$ (0.21)	\$ (2.01)	\$ (0.12)
Loss per share Diluted	\$ (1.68)	\$ (0.21)	\$ (2.01)	\$ (0.12)
Weighted average number of shares used in computing earnings per share:				
Basic	8,256	8,256	8,256	8,256
Diluted	8,256	8,256	8,256	8,256

See accompanying notes.

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**ATLANTIS PLASTICS, INC.  
CONSOLIDATED BALANCE SHEETS**

	<b>September 30, 2007<sup>(1)</sup></b>	<b>December 31, 2006</b>
<i>(In thousands, except share and per share data)</i>		
<b>ASSETS</b>		
Cash and cash equivalents	\$ 457	\$ 59
Accounts receivable (net of allowances of \$1,020 and \$1,280, respectively)	59,494	48,999
Inventories, net	32,804	36,999
Other current assets	6,563	5,479
Deferred income tax assets	2,270	3,108
<b>Total current assets</b>	<b>101,588</b>	<b>94,644</b>
Property and equipment, net	62,913	68,979
Goodwill, net of accumulated amortization and impairment	41,738	54,592
Other assets	7,780	8,673
<b>Total assets</b>	<b>\$214,019</b>	<b>\$226,888</b>
<b>LIABILITIES AND STOCKHOLDERS DEFICIT</b>		
Accounts payable and accrued expenses	\$ 35,790	\$ 31,248
Current maturities of long-term debt	214,119	1,741
<b>Total current liabilities</b>	<b>249,909</b>	<b>32,989</b>
Long-term debt		205,010
Deferred income tax liabilities	3,456	12,043
Other liabilities	1,964	1,039
<b>Total liabilities</b>	<b>255,329</b>	<b>251,081</b>
Commitments and contingencies		
Stockholders' deficit:		
Class A Common Stock, \$.0001 par value, 20,000,000 shares authorized, 6,141,009 shares issued and outstanding in 2007 and 2006	1	1
Class B Common Stock, \$.0001 par value, 7,000,000 shares authorized, 2,114,814 shares issued and outstanding in 2007 and 2006		
Additional paid-in capital	791	390
Note receivable from employee loan		(275)
Accumulated other comprehensive income (net of taxes of \$179 and \$706, respectively)	527	1,373
Accumulated deficit	(42,629)	(25,682)
<b>Total stockholders' deficit</b>	<b>(41,310)</b>	<b>(24,193)</b>

<b>Total liabilities and stockholders deficit</b>	<b>\$214,019</b>	<b>\$226,888</b>
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(1) *Unaudited*

See accompanying notes.

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**ATLANTIS PLASTICS, INC.**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**

<i>(In thousands) (Unaudited)</i>	<b>Nine Months Ended September 30,</b>	
	<b>2007</b>	<b>2006</b>
<b>Operating Activities:</b>		
Net loss	\$(16,598)	\$ (964)
Adjustments to reconcile net loss to net cash used for operating activities:		
Depreciation and non-compete amortization	10,868	9,205
Goodwill impairment charge	12,854	
Loan fee amortization	929	698
Amortization of gain realized on swap recoupon	(1,241)	(650)
Share-based compensation expense	401	284
Loss on disposal of assets	13	
Deferred (tax benefit) income taxes	(7,221)	57
Change in operating assets and liabilities:		
Accounts receivable, net	(10,495)	(675)
Inventories, net	4,195	(157)
Other current assets	(1,084)	(614)
Accounts payable and accrued expenses	4,542	(10,849)
Other assets and liabilities	475	(1,566)
Net cash used for operating activities	(2,362)	(5,231)
<b>Investing Activities:</b>		
Capital expenditures	(4,937)	(8,194)
Proceeds from asset disposals	212	
Net cash used for investing activities	(4,725)	(8,194)
<b>Financing Activities:</b>		
Net borrowings under revolving credit facility	4,600	11,600
Proceeds from issuance of long-term bonds	4,100	
Repayments under term loans	(600)	(1,200)
Financing costs associated with Credit Facilities	(158)	(140)
Repayments on bonds	(732)	(383)
Proceeds from swap recoupon		3,417
Repayments on notes receivable from employee	275	
Net cash provided by financing activities	7,485	13,294
Net increase (decrease) in cash and cash equivalents	398	(131)
Cash and cash equivalents at beginning of period	59	178

Cash and cash equivalents at end of period	\$ 457	\$ 47
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**Supplemental disclosure of non-cash activities:**

Non-cash increase of accounts receivable and accounts payable in connection with supplier agreements	\$ 23	\$ 908
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See accompanying notes.

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**ATLANTIS PLASTICS, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
(Unaudited)

**Note 1. Basis of Presentation**

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States ( GAAP ) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three and nine-month periods ended September 30, 2007 are not necessarily indicative of the results that may be expected for the year ended December 31, 2007.

The consolidated balance sheet at December 31, 2006 has been derived from the audited consolidated financial statements at that date but does not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements.

The information included in this Form 10-Q should be read in conjunction with Management's Discussion and Analysis and consolidated financial statements and footnotes thereto included in the Atlantis Plastics, Inc. Form 10-K for the year ended December 31, 2006.

Certain reclassifications have been made to prior year amounts to conform to the current presentation format.

In preparing its consolidated financial statements, the Company considered its ability to continue as a going concern due to current quarter and year to date results of operations, availability under our revolving credit facility, and the default that currently exists under its Credit Facilities. The Company believes that it will be successful in negotiating a waiver and amendment to its Credit Facilities. In addition, the Company has the ability to reduce or delay its capital expenditures and manage its working capital to improve its cash generated from operations. If the repayment of the Company's loans under its Credit Facilities is accelerated and it cannot obtain sufficient additional funds to repay such loans, its business, operating results, financial condition and ability to continue as a going concern would be in substantial doubt. Assuming the payment of its debt is not accelerated, the Company's current projections indicate it will have sufficient cash flows to support its operations, fund working capital and capital expenditures and satisfy debt service requirements.

**Table of Contents****Note 2. Inventories**

Inventories are stated at the lower of cost or market. Market is established based on the lower of replacement cost or estimated net realizable value, with consideration given to deterioration, obsolescence, and other factors. Cost includes materials, direct and indirect labor, and factory overhead and is determined using the first-in, first-out method.

The components of inventory consist of the following at September 30, 2007 and December 31, 2006:

<i>(In thousands)</i>	<b>September 30, 2007</b>	<b>December 31, 2006</b>
Raw materials	\$ 17,292	\$ 20,250
Work in progress	408	560
Finished products	15,913	17,321
Inventory reserves	(809)	(1,132)
Inventories, net	<b>\$ 32,804</b>	<b>\$ 36,999</b>

**Note 3. Loss Per Share Data**

The following table sets forth the computation of basic and diluted loss per share for the periods indicated:

<i>(In thousands, except per share data)</i>	<b>Three Months Ended September 30,</b>		<b>Nine Months Ended September 30,</b>	
	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
Net loss	\$ (13,909)	\$ (1,754)	\$ (16,598)	\$ (964)
Weighted average shares outstanding basic	8,256	8,256	8,256	8,256
Net effect of dilutive stock options based On treasury stock method				
Weighted average shares outstanding diluted	8,256	8,256	8,256	8,256
Loss per share basic	\$ (1.68)	\$ (0.21)	\$ (2.01)	\$ (0.12)
Loss per share diluted	\$ (1.68)	\$ (0.21)	\$ (2.01)	\$ (0.12)

**Table of Contents****Note 4. Comprehensive Loss**

Total comprehensive loss for the three and nine months ended September 30, 2007 and 2006 was as follows:

<i>(In thousands)</i>	<b>Three Months</b>		<b>Nine Months</b>	
	<b>Ended September 30, 2007</b>	<b>2006</b>	<b>Ended September 30, 2007</b>	<b>2006</b>
Net loss as reported	\$ (13,909)	\$ (1,754)	\$ (16,598)	\$ (964)
Unrealized (loss) on derivatives, net of income taxes	(495)	(910)	(847)	(143)
Total comprehensive loss	\$ (14,404)	\$ (2,664)	\$ (17,445)	\$ (1,107)

**Note 5. Long-term Debt**

Long-term debt consisted of the following balances at September 30, 2007 and December 31, 2006:

<i>(In thousands)</i>	<b>September 30, 2007</b>	<b>December 31, 2006</b>
Senior secured term loan	\$ 117,300	\$ 117,900
Junior secured term loan	75,000	75,000
Revolving credit facility	15,500	10,900
Bonds	6,319	2,951
Total debt	214,119	206,751
Less current portion of long-term debt	(2,376)	(1,741)
Less long-term debt classified as current	(211,743)	
Long-term debt	\$	\$ 205,010

On March 22, 2005, the Company entered into two secured credit agreements (the Credit Facilities) provided by a syndicate of financial institutions. The Credit Facilities included a \$120 million senior secured term loan (the Senior Term Loan) maturing September 2011 and a \$25 million revolving credit facility maturing March 2011. The Second Lien Credit Agreement included a \$75 million junior secured term loan (the Junior Term Loan) maturing in 2012. The Company is in default of its Senior Term Loan, revolving credit facility and Junior Term Loan for violating certain financial covenants. As a result, the Company's lenders have the right to require immediate repayment of the outstanding indebtedness under these loans, the full amount of which consequently has been reclassified as current debt. The Company has been actively working with its lenders to negotiate a waiver of the default or an appropriate amendment to its Credit Facilities. If the Company is unable to reach an arrangement with its lenders, and the repayment of its debt is accelerated, the Company would be required to raise additional funds through the sale of assets, subsidiaries or securities. There can be no assurance that any of these sources of funds would be available in amounts sufficient for the Company to meet its obligations or on acceptable terms. If the repayment of the Company's loans under its Credit Facilities is

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accelerated and it cannot obtain sufficient additional funds to repay such loans, its business, operating results, financial condition and ability to continue as a going concern would be in substantial doubt.

As of September 30, 2007 the Company had \$6.3 million in industrial development bonds outstanding. The Company is currently in default of these bonds for violating the cross-default provision. Accordingly, the full amount of the bonds has been reclassified as current debt.

On June 6, 2005, the Company entered into an interest rate swap contract with a notional amount of \$125 million to effectively fix the interest rate on a portion of its floating rate debt. This contract had the effect of converting a portion of the Company's floating rate debt to a fixed 30-day LIBOR of 3.865%, plus the applicable spread. The interest rate swap was to expire on June 6, 2008. On May 16, 2006, the Company terminated this swap realizing \$3.4 million upon termination, and concurrently entered into a new swap that also terminates on June 6, 2008. The \$3.4 million is being amortized monthly as an offset to interest expense over the life of the original swap. Cash flows from the termination of this interest rate swap are classified as financing activities, the same category as the cash flows from the items being hedged. The new contract, which has substantially identical terms as the terminated contract, has the effect of converting a portion of the Company's floating rate debt to a fixed 30-day LIBOR of 5.265%, plus the applicable spread. The fair value of the Company's interest rate swap agreement is the estimated amount that the Company would receive or pay to terminate the agreement at the reporting date, taking into account the current interest rate environment and the remaining term of the interest rate swap agreement. The fair value of the interest rate swap outstanding at September 30, 2007 was a long-term liability of approximately \$403,000, and the change in fair value was recorded as part of other comprehensive income, net of income taxes (see also Note 4, Comprehensive Loss; Note 7, Capital Structure; and Note 8, Derivative Instruments and Hedging Activities).

**Note 6. Stock-based Compensation**

The Company's amended 2001 Stock Award Plan allows the granting of 865,000 of stock-based awards, including stock options, stock appreciation rights, restricted stock, stock units, bonus stock, dividend equivalents, other stock related awards and performance awards that may be settled in cash, stock, or other property. In the first nine months of 2007, the Company granted 370,000 stock options, and recognized share-based expense of \$401,000. There are a total of 805,000 options outstanding as of September 30, 2007.

**Table of Contents****Note 7. Capital Structure**

The Company's capital stock consists of Class A Common Stock, with holders entitled to one vote per share, and Class B Common Stock, with holders entitled to 10 votes per share. Holders of the Class B Common Stock are entitled to elect 75% of the Board of Directors; holders of Class A Common Stock are entitled to elect the remaining 25%. Each share of Class B Common Stock is convertible, at the option of the holder thereof, into one share of Class A Common Stock. Class A Common Stock is not convertible into shares of any other equity security. During the nine months ended September 30, 2007 and 2006, zero shares of Class B Common Stock were converted into Class A Common Stock.

The following table summarizes changes in Stockholders' Deficit during the nine months ended September 30, 2007:

<i>(In thousands)</i>	Class A Common Stock	Class B Common Stock	Additional Paid-In Capital	Accum- ulated Deficit	Note Receivable	Accumulated Other Compre- hensive Income	Total Stockholders Deficit
<b>Balance at January 1, 2007</b>	<b>\$1</b>	<b>\$</b>	<b>\$390</b>	<b>\$(25,682)</b>	<b>\$(275)</b>	<b>\$1,373</b>	<b>\$(24,193)</b>
Net loss				(16,598)			(16,598)
Change in fair value of derivatives, net of \$508 income tax benefit						(846)	(846)
Cumulative effect of FIN48, net of \$201 income tax benefit				(349)			(349)
Repayment of employee loan					275		275
Share-based compensation			401				401
<b>Balance at September 30, 2007</b>	<b>\$1</b>	<b>\$</b>	<b>\$791</b>	<b>\$(42,629)</b>	<b>\$</b>	<b>\$ 527</b>	<b>\$(41,310)</b>

**Note 8. Derivative Instruments and Hedging Activities**

All derivatives are recorded on the consolidated balance sheets at fair value. On the date the derivative contract is entered into, the Company designates the derivative as either (1) a fair value hedge of a recognized liability, (2) a cash flow hedge of a forecasted transaction, (3) the hedge of a net investment in a foreign operation, or (4) a non-designated derivative instrument. The Company is engaged in an interest rate swap agreement that is classified as a cash flow hedge. Changes in the fair value of derivatives that are classified as a cash flow hedge are recorded in other comprehensive income until reclassified into earnings at the time of settlement of the hedged transaction.

The Company formally documents all relationships between hedging instruments and hedged items as well as the risk management objectives and strategy. The Company formally assesses, both at the hedge's inception and on an ongoing basis, whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in the hedged items. The Company does not utilize derivatives for speculative purposes.

**Table of Contents****Note 9. Segment Information**

The Company has three operating segments: Plastic Films, Injection Molding, and Profile Extrusion. Information related to such segments is as follows:

<i>(in thousands)</i>	<b>Three Months Ended September 30, 2007</b>				
	<b>Plastic Films</b>	<b>Injection Molding</b>	<b>Profile Extrusion</b>	<b>Corporate</b>	<b>Consolidated</b>
Net sales	\$69,869	\$26,307	\$ 7,368	\$	\$103,544
Operating income (loss)	1,850	(154)	(12,741) <sup>(1)</sup>		(11,045)
Capital expenditures	455	310	29	108	902
Depreciation and non-compete amortization	1,774	1,001	368	240	3,383

<i>(in thousands)</i>	<b>Three Months Ended September 30, 2006</b>				
	<b>Plastic Films</b>	<b>Injection Molding</b>	<b>Profile Extrusion</b>	<b>Corporate</b>	<b>Consolidated</b>
Net sales	\$71,114	\$29,133	\$8,014	\$	\$108,261
Operating income (loss)	2,088	1,103	(876)		2,315
Capital expenditures	1,653	453	353	292	2,751
Depreciation and non-compete amortization	1,302	1,171	322	290	3,085

<sup>(1)</sup> Includes \$12.9 million of goodwill impairment charge.

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	<b>Nine Months Ended September 30, 2007</b>				
<i>(in thousands)</i>	<b>Plastic Films</b>	<b>Injection Molding</b>	<b>Profile Extrusion</b>	<b>Corporate</b>	<b>Consolidated</b>
Net sales	\$202,218	\$83,437	\$ 22,759	\$	\$308,414
Operating income (loss)	10,887	(1,822)	(12,727) <sup>(1)</sup>		(3,662)
Capital expenditures	3,007	1,443	167	320	4,937
Depreciation and non-compete amortization	4,762	4,162	1,054	890	10,868
	<b>Nine Months Ended September 30, 2006</b>				
<i>(in thousands)</i>	<b>Plastic Films</b>	<b>Injection Molding</b>	<b>Profile Extrusion</b>	<b>Corporate</b>	<b>Consolidated</b>
Net sales	\$207,891	\$94,000	\$26,757	\$	\$328,648
Operating income (loss)	8,135	5,389	(496)		13,028
Capital expenditures	4,268	2,086	1,498	342	8,194
Depreciation and non-compete amortization	3,953	3,472	895	885	9,205
<b>Identifiable assets</b> <i>(in thousands)</i>	<b>Plastic Films</b>	<b>Injection Molding</b>	<b>Profile Extrusion</b>	<b>Corporate</b>	<b>Consolidated</b>
At September 30, 2007	\$149,139	\$103,401	\$31,464	\$(69,985) <sup>(2)</sup>	\$214,019
At December 31, 2006	\$140,318	\$107,676	\$45,918	\$(67,024) <sup>(2)</sup>	\$226,888

(1) Includes \$12.9 million of goodwill impairment charge.

(2) Corporate identifiable assets are primarily intercompany balances that eliminate when combined with other segments.

**Table of Contents****Note 10. New Accounting Standards**

In June 2006, the Financial Accounting Standards Board ( FASB ) issued FIN 48, *Accounting for Uncertainty in Income Taxes – an interpretation of FASB Statement No. 109* ( FIN 48 ). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with Statement of Financial Accounting Standards No. 109, *Accounting for Income Taxes*. FIN 48 prescribes a recognition and measurement threshold for an enterprise to report tax positions in their financial statements. Under FIN 48 an enterprise must also make extensive disclosures about tax positions that do not qualify for financial statement recognition.

The evaluation of a tax position in accordance with FIN 48 is a two-step process. The first step is recognition: the enterprise determines whether it is more likely than not likely that a tax position will be sustained upon examination. The second step is measurement: a tax position that meets the more-likely-than-not recognition threshold is measured to determine the amount of expense or benefit to recognize in the financial statements. FIN 48 is effective for fiscal years beginning after December 15, 2006.

The Company adopted the provisions of FIN 48 on January 1, 2007. Among other things, FIN 48 requires application of a more likely than not threshold to the recognition and derecognition of tax positions. It further requires that a change in judgment related to prior years' tax positions be recognized in the quarter of such change. As a result of the implementation of FIN 48, the Company recognized an increase of approximately \$349,000 (net of \$203,000 income tax benefit) in the liability for unrecognized tax benefits, which was accounted for as a reduction to the January 1, 2007 balance of accumulated deficit. A reconciliation of the beginning and ending amounts of unrecognized tax benefits is as follows:

Balance at January 1, 2007	\$ 655,000
Additions based on tax positions related to current year	104,000
Additions for tax positions of prior years	
Reductions for tax positions of prior years	
Settlements	
Balance at September 30, 2007	\$ 759,000

The Company or one of its subsidiaries files income tax returns in the U.S. federal jurisdiction, and various states and foreign (Canada) jurisdictions. The Company is not currently subject to U.S. federal, state or local, or non-U.S. income tax examinations by tax authorities for any tax years. Therefore the Company believes that there is no tax jurisdiction in which the outcome of unresolved issues or claims is likely to be material to its financial position, cash flows or results of operations. The Company further believes that it has made adequate provision for all income tax uncertainties. With few exceptions, the Company is no longer subject to United States federal, state and local income tax examinations for years ended before 2004 or before 2003 for non-United States income tax examinations.

At January 1, 2007, the Company's unrecognized tax benefits – that is, the aggregate tax effect of differences between tax return positions and the benefits recognized in the Company's financial statements as shown above amounted to \$655,000. This amount increased to \$759,000 during the nine months ended September 30, 2007. If recognized, all of the Company's unrecognized tax benefits would reduce its income tax expense and effective tax rate. No portion of any such reduction may be reported as discontinued operations.



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During 2007, certain factors could potentially reduce the Company's unrecognized tax benefits, either because of the expiration of open statutes of limitation or modifications to the Company's intercompany accounting policies and procedures. Each of these tax positions would affect the Company's total tax provision or effective tax rate.

The Company classifies interest on tax deficiencies as tax expense and also classifies income tax penalties as tax expense. At January 1, 2007, before any tax benefits, the Company's accrued interest on unrecognized tax benefits amounted to \$93,000 and it had recorded no related accrued penalties. The amount of accrued interest increased by \$31,000 during the nine months ended September 30, 2007 to \$124,000.

In September 2006, the FASB issued Statement of Financial Accounting Standard No. 157 (SFAS 157), which defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. The provisions of SFAS 157 are effective as of the beginning of the Company's 2008 fiscal year. The Company is currently evaluating the impact of adopting SFAS 157 on its consolidated financial statements.

In February 2007, the FASB issued Statement of Financial Accounting Standards No. 159 (SFAS 159), *The Fair Value Option for Financial Assets and Financial Liabilities - Including an Amendment of FASB Statement No. 115*. SFAS 159 permits, but does not require, companies to report at fair value the majority of recognized financial assets, financial liabilities and firm commitments. Under this standard, unrealized gains and losses on items for which the fair value option is elected are reported in earnings at each subsequent reporting date. The Company is currently assessing the effect SFAS No. 159 may have, if any, on its consolidated financial statements when it becomes effective on January 1, 2008.

**Note 11. Severance and Restructuring Expense**

On January 29, 2007, the Company closed its Warren, Ohio Injection Molding facility, and transferred the majority of the assets and business to other Company facilities. The Company expects to incur between \$2.0 million and \$2.2 million in total costs associated with this plant closure. The book value of its owned Warren, Ohio facility was approximately \$1.3 million on January 31, 2007. The Company recorded accelerated depreciation of this asset in the first half of 2007 of approximately \$1.1 million, and completed the sale of the facility during the third quarter of 2007. The Company recorded contract termination costs of approximately \$0.1 million for the remaining lease payments on a 25,000 square foot warehouse lease that expires on January 31, 2009. In connection with the closure of the Warren, Ohio facility, the Company incurred severance costs of \$0.1 million for the severance of 35 employees, which was substantially paid in cash during the first half of 2007. Included in its estimate of expected total closure costs are an aggregate of up to between \$0.7 million and \$0.9 million in 2007 for expenses of moving inventory and equipment, employee relocation, and costs associated with transitioning customer deliveries in a manner designed to avoid disruptions in customer orders. These costs will be paid in cash and charged to expense in the period in which they are incurred.

In the first nine months of 2007, the Company incurred severance and restructuring expense of \$1.1 million. This was comprised of \$953,000 in severance and restructuring expense associated with the Company's closure of its Warren, Ohio facility and \$166,000 in severance expense related to other facilities. As of September 30, 2007, the unpaid portion of severance expense associated with its former Chief Executive

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Officer and certain other employees was approximately \$168,000 and is included in accrued expenses in the accompanying consolidated balance sheet.

**Note 12. Goodwill**

Goodwill represents the excess of the purchase price of our acquisitions over the fair value of the assets acquired. The changes in the carrying amount of goodwill for the nine months ended September 30, 2007, follow (in thousands):

<i>(In thousands)</i>	<b>Plastic Films</b>	<b>Injection Molding</b>	<b>Profile Extrusion</b>	<b>Total</b>
Balance at December 31, 2006	\$31,101	\$10,637	\$ 12,854	\$ 54,592
Goodwill impairment charge			(12,854)	(12,854)
Balance at September 30, 2007	\$31,101	\$10,637	\$	\$ 41,738

Analysis of the potential impairment of goodwill requires a two-step process, as stated in Statement of Financial Accounting Standards No. 142, *Goodwill and Other Intangible Assets*. The first step is the estimation of the fair value of each reporting unit. If step one indicates that impairment potentially exists, the second step is performed to measure the amount of the impairment, if any. Goodwill impairment exists when the estimated fair value of goodwill is less than its carrying value. At September 30, 2007, the Company completed the first step of its goodwill impairment analysis.

The Company estimated the fair value of its reporting units based on a discounted projection of future cash flows, supported with a market based valuation of the Company as a whole. The Plastic Films and Injection Molding reporting units passed the first step analysis and accordingly the Company concluded there was no need to perform a second step analysis for these units. However, the Profile Extrusion reporting unit did not pass the first step analysis. The Company concluded that an impairment loss was probable and could be reasonably estimated for the Profile Extrusion reporting unit. Based on these results, the goodwill balances were impaired as noted in the table above. The total impact of the goodwill impairment estimate in the three months and nine months ended September 30, 2007 was \$12.9 million. There were no such impairments in 2006.

The Company is still in the process of finalizing the second step of the goodwill analysis for the Profile Extrusion reporting unit and expects to complete the full evaluation during the fourth quarter of fiscal 2007. There could be adjustments to the preliminary goodwill impairment charge once the second step of the goodwill impairment analysis is further refined and completed. These impairments and adjustments could be material. Any adjustments to the Company's preliminary estimates as a result of completing this evaluation will be recorded in the consolidated financial statements and disclosed in the annual report of Form 10-K for the year ended December 31, 2007.

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**Note 13. Income Taxes**

In accordance with Statement of Financial Accounting Standards No. 109, *Accounting for Income Taxes*, the Company recorded \$2.1 million of income tax expense during the nine months ended September 30, 2007 due to a \$6.2 million permanent difference between the tax basis and book basis of goodwill.

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

**Overview**

Atlantis Plastics, Inc., headquartered in Atlanta, Georgia, is a leading manufacturer of specialty plastic films and custom injection molded and extruded plastic products with 14 manufacturing plants located throughout the United States. We operate through three operating business segments: Plastic Films, Injection Molding, and Profile Extrusion.

Plastic Films is a leading manufacturer of specialty plastic films. Three operating divisions comprise the Plastic Films segment: (1) Stretch Films, (2) Custom Films, and (3) Institutional Products. Stretch Films produces high quality, monolayer and multilayer plastic films used to cover, package and protect products for storage and transportation applications, i.e. for palletization. We are, with our Linear brand, one of the two original producers and one of the largest producers of stretch film in North America. Custom Films produces customized monolayer and multilayer films used as converter sealant webs, acrylic masking, industrial packaging and in laminates for foam padding of carpet, automotive and medical applications. Institutional Products converts custom films into disposable products such as table covers, gloves and aprons, which are used primarily in the institutional food service industry.

Injection Molding is a leading manufacturer of both custom and proprietary injection molded products. Injection Molding produces a number of custom injection molded components that are sold primarily to original equipment manufacturers, or OEMs, in the home appliance, and automotive parts industries. Injection Molding also manufactures a line of proprietary injection molded siding panels for the home building and remodeling markets.

Profile Extrusion manufactures custom profile extruded plastic products, primarily for use in both trim and functional applications in commercial and consumer products, including mobile homes, residential doors and windows, office furniture and appliances, and recreational vehicles, where we have a leading market share.

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Selected income statement data for the quarterly periods ended March 31, 2006 through September 30, 2007 are as follows (in millions):

<i>(In millions)</i>	Q3	2007 Q2	Q1	Year	Q4	2006 Q3	Q2	Q1
<b>PLASTIC FILMS VOLUME</b>								
(pounds)	69.6	70.9	71.1	257.0	58.3	69.3	69.3	60.1
<b>NET SALES</b>								
Plastic Films	\$ 69.8	\$ 68.0	\$ 64.4	\$266.9	\$59.0	\$ 71.1	\$ 68.7	\$ 68.1
Injection Molding	26.3	28.8	28.3	118.9	24.9	29.2	32.6	32.2
Profile Extrusion	7.4	7.9	7.5	32.9	6.1	8.0	9.3	9.5
Total	\$103.5	\$104.7	\$100.2	\$418.7	\$90.0	\$108.3	\$110.6	\$109.8
<b>GROSS MARGIN</b>								
Plastic Films	11%	14%	16%	11%	11%	11%	11%	13%
Injection Molding	6%	7%	5%	13%	9%	12%	13%	16%
Profile Extrusion	14%	15%	15%	7%	1%	1%	14%	8%
Total	10%	12%	13%	11%	9%	10%	12%	13%
<b>OPERATING MARGIN</b>								
Plastic Films	3%	6%	8%	4%	2%	3%	4%	5%
Injection Molding	-1%	-2%	-3%	5%	2%	4%	5%	8%
Profile Extrusion	-173%	-1%	1%	-4%	-14%	-11%	4%	0%
Total	-11%	3%	4%	3%	1%	2%	4%	5%

**Results of Operations****Net Sales**

Net sales for the quarter and nine months ended September 30, 2007 were \$103.5 million and \$308.4 million, respectively, compared to \$108.3 million and \$328.6 million, respectively, for the comparable periods in 2006. These decreases are a result of a decrease in net sales in each of our three business segments.

Net sales for the Plastic Films segment decreased 2% to \$69.8 million for the third quarter of 2007 compared to \$71.1 million for the third quarter of 2006. Net sales for the nine months ended September 30, 2007 decreased 3% to \$202.2 million compared to \$207.9 million for the same period in 2006. These decreases are reflective of lower average selling prices. Sales volume (measured in pounds) for the third quarter remained flat and increased 6% for the nine months in comparison to the prior year.

Net sales for the Injection Molding segment for the quarter and nine months ended September 30, 2007 decreased 10% and 11%, respectively, compared to the quarter and nine months ended September 30, 2006. These decreases are primarily attributable to weakness in the housing sector.

Net sales for the Profile Extrusion segment decreased 8% and 15%, respectively, for the quarter and nine months ended September 30, 2007 compared to the same periods in 2006. These decreases are primarily due to weakness in the housing and recreational vehicle markets.



**Table of Contents****Gross Margin and Operating Margin**

Gross margin remained static at 10% for the quarter ended September 30, 2007 compared to the quarter ended September 30, 2006. Gross margin decreased to 11% for the nine months ended September 30, 2007 from 12% for the nine months ended September 30, 2006. Operating margins were (11%) and (1%) for the quarter and nine months ended September 30, 2007 compared to 2% and 4% for the quarter and nine months ended September 30, 2006. Excluding the effect of goodwill impairment, operating margins were 2% and 3%, respectively, for the quarter and nine months ended September 30, 2007.

In the Plastic Films segment, gross margin and operating margin for the quarter ended September 30, 2007 remained flat at 11% and 3%, respectively, compared with the quarter ended September 30, 2006. For the nine months ended September 30, 2007, gross margin and operating margin increased to 13% and 5%, respectively, from 12% and 4%, respectively, for the comparable periods in 2006. These increases are primarily the result of higher utilization rates and expansion of our value-added product line.

In the Injection Molding segment, gross margin was 6% for the quarter ending September 30, 2007 and 12% for the quarter ending September 30, 2006, and operating margin decreased to (1%) for the quarter ending September 30, 2007 compared with 4% for the quarter ending September 30, 2006. For the nine months ended September 30, 2007, gross margin decreased from 14% to 6% and operating margin decreased from 6% to (2%). These declines are due primarily to weakness in the housing sector, costs incurred to close our Warren, Ohio manufacturing facility and operational inefficiencies at our Alamo, Texas plant.

In the Profile Extrusion segment, gross margin and operating margin were 14% and (173%), respectively, for the quarter ended September 30, 2007, compared to 1% and (11%), respectively, for the quarter ended September 30, 2006. For the nine months ended September 30, 2007, gross margin and operating margin were 15% and (56%), respectively, compared to 8% and (2%), respectively, for the same period of 2006. Excluding the effect of the goodwill impairment, operating margins were 2% and 1%, respectively, for the quarter and nine months ended September 30, 2007. Excluding the effect of the goodwill impairment charge, the increases in gross and operating margins were due to operational improvement initiatives that generated reductions in scrap rates and improvements in labor productivity.

**Selling, General and Administrative Expense**

Selling, general and administrative expenses ( SG&A ) remained flat at \$8.2 million for the quarter ended September 30, 2007 compared with the quarter ended September 30, 2006. SG&A for the nine months ended September 30, 2007 were \$25.1 compared with \$25.0 million for the nine months ended September 30, 2007 and 2006.

**Goodwill Impairment Charge**

In the three and nine months ended September 30, 2007, we wrote off \$12.9 million of goodwill in our Profile Extrusion segment as a result of the continuing weakened housing and recreational vehicle markets and accounting valuation techniques in deriving the fair values of our reporting units.

Analysis of the potential impairment of goodwill requires a two-step process, as stated in Statement of Financial Accounting Standards No. 142, *Goodwill and Other Intangible Assets* . The first step is the estimation of the fair value of each reporting unit. If step one indicates that impairment potentially exists, the second step is performed to measure the amount of the impairment, if any. Goodwill impairment exists when

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the estimated fair value of goodwill is less than its carrying value. At September 30, 2007, we completed the first step of our goodwill impairment analysis.

We estimated the fair value of our reporting units based on a discounted projection of future cash flows, supported with a market based valuation of the Company as a whole. The Plastic Films and Injection Molding reporting units passed the first step analysis and accordingly we concluded there was no need to perform a second step analysis for these units. However, the Profile Extrusion reporting unit did not pass the first step analysis. We concluded that an impairment loss was probable and could be reasonably estimated for the Profile Extrusion reporting unit. Based on these results, the goodwill balances were impaired. The total impact of the goodwill impairment estimate in the three months and nine months ended September 30, 2007 was \$12.9 million. There were no such impairments in 2006.

We are still in the process of finalizing the second step of the goodwill analysis for the Profile Extrusion reporting unit and expect to complete the full evaluation during the fourth quarter of fiscal 2007. There could be adjustments to our preliminary goodwill impairment charge once the second step of the goodwill impairment analysis is further refined and completed. These impairments and adjustments could be material. Any further adjustments to our preliminary estimates as a result of completing this evaluation will be recorded in the consolidated financial statements and disclosed in the annual report of Form 10-K for the year ended December 31, 2007.

**Net Interest Expense**

Net interest expense for the quarter and nine months ended September 30, 2007 increased to \$7.1 million and \$18.7 million, respectively, from \$5.1 million and \$14.7 million, respectively, for the same periods in 2006. The increases are primarily due to the recognition of 2% default interest in connection with our Credit Facilities, and to a lesser extent higher debt levels.

**Income Taxes**

In accordance with Statement of Financial Accounting Standards No. 109, *Accounting for Income Taxes*, we recorded \$2.1 million of income tax expense in the third quarter of 2007 due to a \$6.2 million permanent difference between the tax basis and book basis of goodwill.

**Operating and Net Income (Loss)**

As a result of the factors described above, operating income decreased to (\$11.0) million, (11%) of net sales, during the quarter ended September 30, 2007, compared with \$2.3 million, 2% of net sales, for the quarter ended September 30, 2006. For the nine months ended September 30, 2007, operating income decreased to (\$3.7) million, (1%) of net sales, compared to \$13.0 million, 4% of net sales, for the nine months ended September 30, 2006.

Net loss and basic and diluted loss per share for the three months and nine months ended September 30, 2007 and 2006 were as follows:

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	<b>Three Months Ended</b>		<b>Nine Months Ended</b>	
	<b>September 30,</b>		<b>September 30,</b>	
<i>(In thousands, except per share data)</i>	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
Net loss	\$ (13,909)	\$ (1,754)	\$ (16,598)	\$ (964)
Loss per share basic	\$ (1.68)	\$ (0.21)	\$ (2.01)	\$ (0.12)
Loss per share diluted	\$ (1.68)	\$ (0.21)	\$ (2.01)	\$ (0.12)

**Liquidity and Capital Resources**

As of September 30, 2007, we had \$0.5 million in cash and cash equivalents and an additional \$4.4 million of unused availability, net of outstanding letters of credit of approximately \$5.1 million, under our senior secured credit facility. Our Credit Facilities includes a \$25 million revolving credit facility maturing March 2011, a \$120 million senior secured term loan maturing in September 2011 and a \$75 million junior secured term loan maturing in March 2012. Substantially all of our accounts receivable, inventories and property and equipment are pledged as collateral under the Credit Facilities.

We are in default of certain financial ratio covenants under our Credit Facilities. During the current quarter, the lenders exercised their right to charge default interest of two percentage points per annum above the applicable rates of interest. In connection with the default, our lenders have the right to require immediate repayment of the outstanding loans under the Credit Facilities. As of September 30, 2007, we had \$207.8 million in outstanding indebtedness under the Credit Facilities, all of which has been reclassified on our balance sheet as current debt as a result of our ongoing loan default.

As of September 30, 2007 we had \$6.3 million in industrial development bonds outstanding. We are currently in default of these bonds for violating the cross-default provision. Accordingly, the full amount of the bonds has been reclassified as current debt.

We have been actively working with our lenders to negotiate a waiver of the default or an appropriate amendment to our Credit Facilities. However, we cannot assure you that we will be able to obtain such a waiver or amendment. If we are unable to reach an arrangement with our lenders, and the repayment of our debt is accelerated, we would be required to raise additional funds through the sale of assets, subsidiaries or securities. There can be no assurance that any of these sources of funds would be available in amounts sufficient for us to meet our obligations or on acceptable terms. If the repayment of our loans under our Credit Facilities is accelerated and we cannot obtain sufficient additional funds to repay such loans, our business, operating results, financial condition and ability to continue as a going concern would be in substantial doubt. If we are able to negotiate an arrangement with our lenders, such arrangement may involve the conversion of all or a portion of our debt to equity, the issuance of securities or other similar transactions that could result in material dilution to existing stockholders. If we issue equity securities in connection with any such arrangement or additional financing, the percentage ownership of our current stockholders may be materially reduced, and such equity securities may have rights, preferences or privileges senior to those applicable to our current stockholders.

Our high debt level and our debt covenants present substantial risks and have negative consequences. For example, they have (1) required us to dedicate all or a substantial portion of our cash flow from operations to debt service, limiting the availability of cash for other purposes; (2) increased our vulnerability to adverse general economic conditions; (3) caused us to be currently out of compliance with certain of our debt covenants and thereby adversely impacted our ability to borrow additional funds to maintain our operations if we suffer shortfalls in net sales; (4) hindered our flexibility in planning for, or reacting to, changes in our business and industry by preventing us from borrowing money to upgrade equipment or facilities; and (5) impaired our ability to obtain additional financing in the future for working capital, capital expenditures, acquisitions, or general corporate purposes.



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In preparing our consolidated financial statements, we considered our ability to continue as a going concern due to current quarter and year to date results of operations, availability under our revolving credit facility, and the default that currently exists under our Credit Facilities and industrial development bonds. We believe that we will be successful in negotiating a waiver and amendment to our Credit Facilities. In addition, we have the ability to reduce or delay our capital expenditures and manage our working capital to improve our cash generated from operations. Assuming the repayment of our debt is not accelerated, our current projections indicate we will have sufficient cash flows to support our operations, fund working capital and capital expenditures and satisfy debt service requirements.

***Cash Flows from Operating Activities***

Net cash used for operating activities was \$2.4 million in the nine months ended September 30, 2007, compared to \$5.2 million for the same period in 2006. The use of operating cash flow during 2007 was comprised of \$10.5 million increase in accounts receivable, a decrease of \$7.2 million in deferred tax benefit, \$1.2 million in amortization of a gain realized on a swap recoupon, and \$1.1 million increase in other current assets; partially offset by \$12.9 million of a goodwill impairment charge, \$10.9 million of depreciation and non-compete amortization, \$4.5 million increase in accounts payable and accrued expenses, \$4.2 million reduction in net inventories, \$0.9 million in loan fee amortization, \$0.5 million decrease in other assets and liabilities and \$0.4 million in non-cash share-based compensation expense. The use of operating cash flow during the same period in 2006 was attributable to a \$10.9 million reduction in accounts payable and accrued expenses, a \$1.6 million increase in other assets and liabilities, a \$0.7 million increase in accounts receivable, amortization of \$0.7 million for a redeemed swap, \$0.6 million increase in other current assets and a \$0.2 million increase in net inventories; partially offset by \$9.2 million in depreciation and \$0.7 million of loan fee amortization, \$0.3 million in non-cash share-based compensation expense, and \$0.1 million in deferred income taxes.

***Cash Flows from Investing Activities***

Net cash used for investing activities decreased to \$4.7 million in the nine months ended September 30, 2007, compared to \$8.2 million for the same period in 2006 resulting from decreased capital expenditures between periods.

***Cash Flows from Financing Activities***

Net cash provided by financing activities in the nine months ended September 30, 2007 was \$7.5 million compared to \$13.3 million for the for the same period in 2006. Net cash provided by financing activities for the first nine months of 2007 resulted from net borrowings of \$4.6 million under the revolving credit facility, \$4.1 million from the issuance of long-term bonds and \$0.3 million in repayments from an employee loan; partially offset by \$0.7 million in repayments on bonds, \$0.6 million of repayments on term loans, and \$0.2 million in financing costs associated with the Credit Facilities. Net cash provided by financing activities in the first nine months of 2006 was resulted from net borrowings of \$11.6 million under the revolving credit facility and proceeds of \$3.4 million from the swap redemption, partially offset by \$1.2 million of repayments on debt, \$0.4 million repayments on bonds and \$0.1 million in financing costs associated with credit agreements.

***Recent Accounting Pronouncements***

In June 2006, the Financial Accounting Standards Board ( FASB ) issued FIN 48, *Accounting for Uncertainty in Income Taxes – an interpretation of FASB Statement No. 109* ( FIN 48 ). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise s financial statements in accordance

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with Statement of Financial Accounting Standards No. 109, *Accounting for Income Taxes*. FIN 48 prescribes a recognition and measurement threshold for an enterprise to report tax positions in their financial statements. Under FIN 48 an enterprise must also make extensive disclosures about tax positions that do not qualify for financial statement recognition.

The evaluation of a tax position in accordance with FIN 48 is a two-step process. The first step is recognition: the enterprise determines whether it is more likely than not likely that a tax position will be sustained upon examination. The second step is measurement: a tax position that meets the more-likely-than-not recognition threshold is measured to determine the amount of expense or benefit to recognize in the financial statements. FIN 48 is effective for fiscal years beginning December 15, 2006.

We adopted the provisions of FIN 48 on January 1, 2007. Among other things, FIN 48 requires application of a more likely than not threshold to the recognition and derecognition of tax positions. It further requires that a change in judgment related to prior years tax positions be recognized in the quarter of such change. As a result of the implementation of FIN 48, we recognized an increase of approximately \$349,000 (net of \$203,000 of tax benefit) in the liability for unrecognized tax benefits, which was accounted for as a reduction to the January 1, 2007 balance of accumulated deficit. A reconciliation of the beginning and ending amounts of unrecognized tax benefits is as follows:

Balance at January 1, 2007	\$ 655,000
Additions based on tax positions related to current year	104,000
Additions for tax positions of prior years	
Reductions for tax positions of prior years	
Settlements	
Balance at September 30, 2007	\$ 759,000

We file income tax returns in the U.S. federal jurisdiction, and various states and foreign (Canada) jurisdictions. We are not currently subject to U.S. federal, state or local, or non-U.S. income tax examinations by tax authorities for any tax years. Therefore we believe that there is no tax jurisdiction in which the outcome of unresolved issues or claims is likely to be material to our financial position, cash flows or results of operations. We further believe that we have made adequate provision for all income tax uncertainties. With few exceptions, we are no longer subject to United States federal, state and local income tax examinations for years ended before 2004 or before 2003 for non-United States income tax examinations.

At January 1, 2007, our unrecognized tax benefits that is, the aggregate tax effect of differences between tax return positions and the benefits recognized in our financial statements as shown above amounted to \$655,000. This amount increased to \$759,000 during the nine months ended September 30, 2007. If recognized, all of our unrecognized tax benefits would reduce our income tax expense and effective tax rate. No portion of any such reduction may be reported as discontinued operations. During 2007, certain factors could potentially reduce our unrecognized tax benefits, either because of the expiration of open statutes of limitation or modifications to our intercompany accounting policies and procedures. Each of these tax positions would affect our total tax provision or effective tax rate.

We classify interest on tax deficiencies as tax expense and also classify income tax penalties as tax expense. At January 1, 2007, before any tax benefits, our accrued interest on unrecognized tax benefits

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amounted to \$93,000 and we had recorded no related accrued penalties. The amount of accrued interest increased by \$31,000 during the nine months ended September 30, 2007 to \$124,000.

In September 2006, the FASB issued Statement of Financial Accounting Standard No. 157 ( SFAS 157 ), which defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. The provisions of SFAS 157 are effective as of the beginning of the Company's 2008 fiscal year. We are currently evaluating the impact of adopting SFAS 157 on our consolidated financial statements.

In February 2007, the FASB issued Statement of Financial Accounting Standards No. 159 ( SFAS 159 ), *The Fair Value Option for Financial Assets and Financial Liabilities Including an Amendment of FASB Statement No. 115* . SFAS 159 permits, but does not require, companies to report at fair value the majority of recognized financial assets, financial liabilities and firm commitments. Under this standard, unrealized gains and losses on items for which the fair value option is elected are reported in earnings at each subsequent reporting date. We are currently assessing the effect SFAS No. 159 may have, if any, on our consolidated financial statements when it becomes effective on January 1, 2008.

**Note Regarding Forward Looking Statements**

This quarterly report on Form 10-Q contains forward-looking statements within the meaning of that term in Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Additional written or oral forward-looking statements may be made from time to time, in press releases, annual or quarterly reports to stockholders, filings with the Securities Exchange Commission, presentations or otherwise. Statements contained herein that are not historical facts are forward-looking statements made pursuant to the safe harbor provisions referenced above.

Forward-looking statements may include, but are not limited to, projections of net sales, income or losses, or capital expenditures; plans for future operations; financing needs or plans; compliance with financial covenants in loan agreements; plans for liquidation or sale of assets or businesses; plans relating to our products or services; assessments of materiality; predictions of future events; the ability to obtain additional financing; our ability to meet obligations as they become due; the impact of pending and possible litigation; as well as assumptions relating to the foregoing. In addition, when used in this discussion, the words anticipates, believes, estimates, expects, intends, and similar expressions are intended to identify forward-looking statements. Forward-looking statements are inherently subject to risks and uncertainties, including, but not limited to, the impact of leverage, dependence on major customers, fluctuating demand for our products, risks in product and technology development, fluctuating resin prices, competition, litigation, labor disputes, capital requirements, and other risk factors detailed in our filings with the Securities and Exchange Commission, some of which cannot be predicted or quantified based on current expectations.

Consequently, future events and actual results could differ materially from those set forth in, contemplated by, or underlying the forward-looking statements. Readers are cautioned not to place undue reliance on any forward-looking statements contained herein, which speak only as of the date hereof. We do not undertake an obligation to publicly release the result of any revisions to these forward-looking statements that may be made to reflect events or circumstances after the date hereof or to reflect the occurrence of unanticipated events.

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

For a discussion of certain market risks related to the Company, see the Quantitative and Qualitative Disclosures about Market Risk section in the Company's Form 10-K for the fiscal year ended December 31, 2006.

The Company had \$207.8 million in variable rate debt outstanding at September 30, 2007. Currently, the Company has an interest rate swap agreement which matures in June 2008 that has the effect of converting \$125 million of the Company's floating rate debt to a fixed rate. The Company has designated this interest rate swap agreement as a cash flow hedge (see also Note 5, Long-term Debt; and Note 8, Derivative Instruments and Hedging Activities). The Company uses interest rate swap agreements to manage its exposure to interest rate changes on the Company's variable rate debt. Based on the Company's variable-rate obligations outstanding at September 30, 2007, a 25 basis point increase or decrease in the level of interest rates would, respectively, increase or decrease annual interest expense by approximately \$0.5 million. Such potential increases or decreases are based on certain simplifying assumptions, including a constant level of variable rate debt for all maturities and an immediate, across-the-board increase or decrease in the level of interest rates with no other subsequent changes for the remainder of the period.

There have been no other significant changes with respect to market risks related to the Company since December 31, 2006.

**Item 4. Controls and Procedures**

Our Chief Executive Officer (CEO) and Chief Financial Officer (CFO) have evaluated the effectiveness of our disclosure controls and procedures as of September 30, 2007. Based on this evaluation, our CEO and CFO have each concluded that our disclosure controls and procedures were ineffective due to the identification of the material weakness in the financial statement close and reporting process described in our 2006 Form 10-K. Notwithstanding the material weakness, management believes the consolidated financial statements included in this report fairly present, in all material respects, our financial condition, results of operations and cash flows for the periods presented. We are in the process of remediating such material weakness and expect to have adequate internal controls in place over the financial statement close and reporting process as of December 31, 2007. The plan to do so is more fully described in our 2006 Form 10-K. (see also Item 1A. Risk Factors)

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*Part II. Other Information*

**Item 1. Legal Proceedings**

The Company is not a party to any legal proceeding other than routine litigation incidental to its business, none of which is material.

**Item 1A. Risk Factors**

*An investment in our common stock involves a high degree of risk. You should carefully consider the factors described below, in addition to those discussed elsewhere in this report, in analyzing an investment in the common stock. If any of the events described below occurs, our business, financial condition and results of operations would likely suffer and the trading price of our common stock could fall.*

*The following factors could cause our actual results to differ materially from those projected in forward-looking statements, whether made in this 10-Q, annual or quarterly reports to shareholders, future press releases, SEC filings or orally, whether in presentations, responses to questions or otherwise. See Note Regarding Forward-Looking Statements.*

**We are in default of our Credit Facilities and industrial development bonds. If our lenders accelerate our loans under our Credit Facilities, our business, operating results, financial condition and ability to continue as a going concern would be in substantial doubt.**

We are in default of certain financial ratio covenants under our Credit Facilities and industrial development bonds. During the current quarter, the lenders exercised their right to charge default interest of two percentage points per annum above the applicable rates of interest. In connection with the default, our lenders have the right to require immediate repayment of the outstanding loans under the Credit Facilities. As of September 30, 2007, we had \$207.8 million in outstanding indebtedness under the Credit Facilities, all of which has been reclassified on our balance sheet as current debt as a result of our ongoing loan default.

As of September 30, 2007 we had \$6.3 million in industrial development bonds outstanding. We are currently in default of these bonds for violating the cross-default provision. Accordingly, the full amount of the bonds has been reclassified as current debt.

From time to time we have amended or revised our financial covenants, and have also received waivers of covenant compliance under various loan arrangements. We have been actively working with our lenders to negotiate a waiver of the default or an appropriate amendment to our Credit Facilities. However, we cannot assure you that we will be able to obtain such a waiver or amendment. If we are unable to reach an arrangement with our lenders, and the repayment of our debt is accelerated, we would be required to raise additional funds through the sale of assets, subsidiaries or securities. There can be no assurance that any of these sources of funds would be available in amounts sufficient for us to meet our obligations or on acceptable terms. If the repayment of our loans under our Credit Facilities is accelerated and we cannot obtain sufficient additional funds to repay such loans, our business, operating results, financial condition and ability to continue as a going concern would be in substantial doubt.

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**Our substantial indebtedness adversely affects our financial condition and could prevent us from fulfilling future obligations.**

As of September 30, 2007 we had \$214.1 million of outstanding indebtedness, approximately \$0.5 million in cash and cash equivalents and an additional \$4.4 million of unused availability under our Credit Facilities, net of outstanding letters of credit of \$5.1 million.

Our substantial indebtedness has negative consequences. For example, it:

increases our vulnerability to general adverse economic and industry conditions;

requires us to dedicate all or a substantial portion of our cash flow from operations to payments on our indebtedness, thereby reducing the availability of our cash flow to fund working capital, capital expenditures, product development efforts and other general corporate purposes;

limits our flexibility in planning for, or reacting to, changes in our business and the industries in which we operate, including our ability to pursue attractive acquisition opportunities;

places us at a competitive disadvantage compared to our competitors that have less debt;

limits our ability to borrow additional funds; and

limits our ability to obtain favorable credit terms.

**We face significant exposure to difficulties in the housing sector.**

Approximately 40% of our sales are to sectors either directly or indirectly tied to the housing and remodeling markets. Products that we produce that are impacted by the economic health of the housing sector include injection molding appliance parts, carpet films, foam lamination films, building panels for siding applications, extruded components for windows and doors, and extruded accessories for the siding industry. The present downturn in the housing sector has negatively affected us, and a sustained downturn in this sector could have a material adverse effect on our business and results of operations.

**We have identified a material weakness in the financial statement close and reporting process.**

Our Chief Executive Officer and Chief Financial Officer concluded that, as of December 31, 2006, our disclosure controls and procedures were ineffective, due to the identification of a material weakness in the financial statement close and reporting process. This material weakness related to: our lack of comprehensive documentation of accounting policies and procedures, our inaccurate preparation and lack of review of reconciliations of certain significant account balances on a timely basis, and our lack of segregation of duties. Failure to adequately remediate this material weakness could result in a material misstatement of the annual or interim consolidated financial statements.

**We face intense competition that could result in our losing or failing to gain market share and adversely affect our results of operations.**

We face intense competition from numerous competitors, several of which have greater financial resources than us. In addition, the markets for certain of our products are characterized by low cost of entry or

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competition based primarily on price. This intense competition could result in pricing pressures, lower sales, reduced margins and lower market share.

Plastic Films competes with a limited number of producers capable of national distribution and a greater number of smaller manufacturers that target specific regional markets and specialty film segments competing on the basis of quality, price, service (including the manufacturer's ability to supply customers in a timely manner) and product differentiation.

Injection Molding competes in a highly fragmented segment of the plastics industry, with a large number of regional manufacturers competing on the basis of customer service (including timely delivery and engineering/design capabilities), quality, product differentiation and price. Our building products business competes with large and well established suppliers to the industry, competing on the basis of product differentiation and service.

Profile Extrusion competes regionally with a number of smaller extruders that focus on specialized niche markets, competing on the basis of cost, quality and service levels.

There can be no assurance that we will continue to compete successfully in the markets for our products or that competition in such markets will not intensify.

**Our financial performance is dependent on raw material prices and our ability to pass on price increases to customers.**

The primary raw materials we use in the manufacture of our products are various plastic resins, primarily polyethylene. Our financial performance therefore is dependent to a substantial extent on the polyethylene resin market. The capacity, supply and demand for plastic resins and the petrochemical intermediates from which they are produced are subject to substantial cyclical price fluctuations and other market disturbances, including supply shortages. Consequently, plastic resin prices may fluctuate as a result of changes in natural gas and crude oil prices. While we attempt to pass through changes in the cost of our raw materials to our customers in the form of price increases, we cannot be assured that we will be able to do so in the future. To the extent that increases in the cost of plastic resins cannot be passed on to our customers, or the duration of time lags associated with a pass through becomes significant, such increases may have a material adverse effect on our profitability. Furthermore, during periods when resin prices are falling, gross profits may suffer, as we will be selling products manufactured with resin purchased one to two months prior at higher prices.

**Sales to one of our customers accounted for 17.4% of our net sales in 2006, and the loss of sales to that customer could harm our business, financial condition and results of operations.**

Sales to Whirlpool Corporation accounted for 17.4% of our net sales in 2006. A significant reduction in Whirlpool's volume, or the loss of Whirlpool as a customer, could have a material adverse effect on our business, financial condition and results of operations.

**Our acquisitions carry risks.**

Acquisitions and investments involve numerous risks such as diversion of senior management's attention, unsuccessful integration of the acquired entity's personnel, operations, technologies and products, lack of market acceptance of new services and technologies or a shift in industry dynamics that negatively impacts the forecasted demand for the new products. Impairment of goodwill and other intangible assets may result if these risks materialize. There can be no assurance that an acquired business will perform as expected or

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generate significant net sales or profits. In addition, acquisitions may involve the assumption of obligations or significant one-time write-offs. In order to finance any future acquisitions, we may need to raise additional funds through public or private financings.

**Our business may suffer if any of our key senior executives discontinues employment with us or if we are unable to recruit and retain highly qualified employees.**

Our future success depends to a large extent on the services of our key managerial employees. We may not be able to retain our executive officers and key personnel or attract additional qualified management in the future. Our business also depends on our continuing ability to recruit, train and retain highly qualified employees. The competition for these employees is intense, and the loss of these employees could harm our business.

**Our intellectual property rights may be inadequate to protect our business.**

We attempt to protect our intellectual property rights through a combination of intellectual property laws, including patents. Our failure to obtain or maintain adequate protection of our intellectual property rights for any reason could have a material adverse effect on our business, results of operations and financial condition.

We also rely on unpatented proprietary technology. It is possible that others will independently develop the same or similar technology or otherwise obtain access to our unpatented technology. If we are unable to maintain the proprietary nature of our technologies, we could be materially adversely affected.

We rely on our trademarks, trade names and brand names to distinguish our products from the products of our competitors, and have registered or applied to register many of these trademarks. There can be no assurance that our trademark applications will be approved. Third parties may also oppose our trademark applications, or otherwise challenge our use of the trademarks. In the event that our trademarks are successfully challenged, we could be forced to rebrand our products, which could result in loss of brand recognition, and could require us to devote resources to advertising and marketing new brands. Further, we cannot be assured that competitors will not infringe our trademarks, or that we will have adequate resources to enforce our trademarks.

**If third parties claim that we infringe upon their intellectual property rights, our operating profits could be adversely affected.**

We face the risk of claims that we have infringed third parties' intellectual property rights. Any claims of patent or other intellectual property infringement, even those without merit, could:

be expensive and time consuming to defend;

cause us to cease making, licensing or using products that incorporate the challenged intellectual property;

require us to redesign, reengineer, or rebrand our products, if feasible;

divert management's attention and resources; or



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require us to enter into royalty or licensing agreements in order to obtain the right to use a third party's intellectual property.

Any royalty or licensing agreements, if required, may not be available to us on acceptable terms or at all. A successful claim of infringement against us could result in our being required to pay significant damages, enter into costly license or royalty agreements, or stop the sale of certain products, any of which could have a negative impact on our operating profits and harm our future prospects.

**If our products infringe on the intellectual property rights of others, we may be required to indemnify our customers for any damages they suffer.**

We generally indemnify our customers with respect to infringement by our products of the proprietary rights of third parties. Third parties may assert infringement claims against our customers. These claims may require us to initiate or defend protracted and costly litigation on behalf of our customers, regardless of the merits of these claims. If any of these claims succeed, we may be forced to pay damages on behalf of our customers or may be required to obtain licenses for the products they use. If we cannot obtain all necessary licenses on commercially reasonable terms, our customers may be forced to stop using our products.

**Environmental, health and safety matters could require material expenditures and changes in our operations.**

We are subject to various environmental, health and safety laws and regulations which govern our operations and which may adversely affect our production costs. Actions by federal, state and local governments concerning environmental, health and safety matters could result in laws or regulations that could increase the cost of producing the products we manufacture or otherwise adversely affect the demand for our products. Certain local governments have adopted ordinances prohibiting or restricting the use or disposal of certain plastic products that are among the types we produce. If such prohibitions or restrictions were widely adopted, it could have a material adverse effect on our business, financial condition and results of operations. In addition, a decline in consumer preference for plastic products due to environmental considerations could have a material adverse effect on our business, financial condition and results of operations.

In addition, certain of our operations are subject to federal, state and local environmental laws and regulations that impose limitations on the discharge of pollutants into the air and water and establish standards for the treatment, storage and disposal of solid and hazardous wastes. Non-compliance could subject us to material liabilities, such as fines, damages, criminal or civil sanctions and remediation costs, or result in interruptions in our operations. We believe our operations are currently in substantial compliance with these laws and regulations. However, there can be no assurance that we have been or will be at all times in compliance with all of these requirements and that the resolution of these environmental matters will not have an adverse effect on our results of operations, financial condition and cash flows in any given period.

Under certain environmental laws, liability for the cleanup of contaminated sites can be imposed retroactively and on a joint and several basis. We could be held responsible for all cleanup costs at a site, whether currently or formerly owned or operated as well as third party sites to which we may have sent waste, and regardless of fault or the legality of the original disposal. While we are not currently aware of contaminated or Superfund sites as to which material outstanding claims or obligations exist, there may be additional sites or contaminants of which we are unaware. The discovery of currently unknown contaminants or the imposition of cleanup obligations could have a material adverse effect on our results of operations or financial condition.

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Environmental laws and regulations are complex, and both the laws and regulations and the interpretation thereof, change frequently and have tended to become more stringent over time. Future developments could restrict or eliminate the use of, or require us to make modifications to our products, which could have a material adverse effect on our results of operations, financial condition and cash flows in any given period. Although we cannot predict with any certainty our future capital expenditure requirements for environmental regulatory compliance, we have not currently identified any of our facilities as requiring major expenditures for environmental remediation or to achieve compliance with environmental regulations. Accordingly, we have not accrued any amounts relating to such expenditures. We do not currently have any insurance coverage for environmental liabilities and do not anticipate obtaining such coverage in the future.

**Our major shareholder has significant influence over our business and could delay, deter or prevent a change of control or other business combination.**

As of December 31, 2006, Earl Powell, our Chairman of the Board, holds approximately 49.5% of our voting power, and is able to exert significant control over our affairs, including the election of a majority of our board, the appointment of our management, the entering into of mergers, sales of substantially all of our assets and other extraordinary transactions. His interests could conflict with those of our other shareholders.

The risks described above are not the only risks facing our Company. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may adversely affect our business, financial condition and/or operating results.

**Item 6. Exhibits**

**(A) EXHIBITS**

31.1 CEO Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

31.2 CFO Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32.1 CEO Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

32.2 CFO Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

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*SIGNATURES*

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

ATLANTIS PLASTICS, INC.

Date: November 19, 2007

**By:** /s/ V. M. Philbrook

V.M. PHILBROOK  
*President and Chief Executive Officer*

Date: November 19, 2007

**By:** /s/ Paul G. Saari

PAUL G. SAARI  
*Senior Vice President, Finance and  
Chief Financial Officer*

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