RAYONIER INC
Form 10-Q/A
November 10, 2014
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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q/A
(AMENDMENT NO. 1)
(Mark One)

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

For the quarterly period ended March 31, 2014
OR

o 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 1-6780
RAYONIER INC.
Incorporated in the State of North Carolina
I.R.S. Employer Identification No. 13-2607329
225 WATER STREET, SUITE 1400
JACKSONVILLE, FL 32202
(Principal Executive Office)
Telephone Number: (904) 357-9100

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

Large accelerated filer x	Accelerated filer o
Non-accelerated filer o	Smaller reporting company o

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

As of November 3, 2014, there were outstanding 126,726,146 Common Shares of the registrant.

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EXPLANATORY NOTE

This Amendment No. 1 (this "Amendment") to the Quarterly Report on Form 10-Q of Rayonier Inc. (the "Company") for the quarterly period ended March 31, 2014 is being filed to amend and restate in their entirety the following items of its Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2014 that was filed on April 30, 2014 (the "Original Filing"): (i) Item 1 of Part I, "Financial Information," (ii) Item 2 of Part I, "Management's Discussion and Analysis of Financial Condition and Results of Operations," and (iii) Item 4 of Part I, "Controls and Procedures". The Company has also updated the signature page, the certifications of its chief executive officer and chief financial officer in Exhibits 31.1, 31.2 and 32 and its unaudited consolidated financial statements formatted in Extensible Business Reporting Language (XBRL) in Exhibit 101. Concurrently with the filing of this Amendment, the Company is also filing Amendment No. 1 to its Annual Report on Form 10-K for the fiscal year ended December 31, 2013, Amendment No. 1 to its Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2014 and Amendment No. 1 to its Form 8-K filed with the Securities and Exchange Commission on July 3, 2014.

On June 27, 2014, the Company spun off its Performance Fibers business to its shareholders as a newly formed publicly traded company named Rayonier Advanced Materials Inc. Following the spin-off, new management conducted a review of the Company's operations and business strategies and identified issues related to its historical timber harvest levels, its estimate of merchantable timber inventory and the effect of such estimate on its calculation of depletion expense in each of the quarterly periods ended March 31, 2014 and June 30, 2014. At the direction of the Company's Board of Directors, management commenced an internal review into these matters with the assistance of independent counsel, forensic accountants and financial advisers. As a result of the internal review, the Company concluded that it included in merchantable timber inventory for 2014, timber in specially designated parcels located in restricted, environmentally sensitive or economically inaccessible areas, which was incorrect, inconsistent with its definition of merchantable timber inventory, and a significant change from prior years. As a result, the Company concluded that it understated its depletion expense in cost of goods sold (referred to as "Cost of sales" in the Company's consolidated statements of income) by approximately $2.0 million in each of the quarterly periods ended March 31, 2014 and June 30, 2014, which resulted in a corresponding overstatement of income from continuing operations of $1.9 million and $2.0 million, respectively, in those periods. In addition, management determined that there was a material weakness in the Company's internal controls related to merchantable timber inventory, as discussed in Part I, Item 4 of this Amendment. Accordingly, the Company has filed this Amendment and the restated interim consolidated financial statements contained herein. Further details of the errors and the impact on the unaudited financial statements set forth in the Original Filing are contained in Note 3 — Restatement of Previously Issued Consolidated Financial Statements in the Notes to the Unaudited Consolidated Financial Statements included in this Amendment.

The Company has not modified or updated disclosures presented in the Original Filing, except to reflect the effects of the restatement of the Company's financial statements and disclose the material weaknesses in our internal control over financial reporting that has been identified since the date of the Annual Report on Form 10-K, as described above. Accordingly, this Amendment does not reflect events occurring after the Original Filing, except as noted above, and this Amendment continues to speak as of the date of the Original Filing. Therefore, this Amendment should be read in conjunction with the Company's other filings made with the Securities and Exchange Commission subsequent to the filing of the Original Filing, including any amendments to those filings.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

RAYONIER INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME
AND COMPREHENSIVE INCOME
(Unaudited)
(Dollars in thousands, except per share amounts)

	Three Months Ended March 31, 2014 (Restated)	2013
SALES	$386,686	$393,719
Costs and Expenses		
Cost of sales	304,619	266,018
Selling and general expenses	15,491	16,099
Other operating expense (income), net (Note 18)	3,537	(3,503)
	323,647	278,614
Equity in income of New Zealand joint venture	—	258
OPERATING INCOME	63,039	115,363
Interest expense	(12,969)	(7,717)
Interest and miscellaneous (expense) income, net	(1,015)	57
INCOME FROM CONTINUING OPERATIONS BEFORE INCOME TAXES	49,055	107,703
Income tax expense	(7,712)	(4,445)
INCOME FROM CONTINUING OPERATIONS	41,343	103,258
DISCONTINUED OPERATIONS, NET (Note 2)		
Income from discontinued operations, net of income tax expense of $0 and $22,273	—	44,477
NET INCOME	41,343	147,735
Less: Net loss attributable to noncontrolling interest	(83)	—
NET INCOME ATTRIBUTABLE TO RAYONIER INC.	41,426	147,735
OTHER COMPREHENSIVE INCOME		
Foreign currency translation adjustment	17,803	975
New Zealand joint venture cash flow hedges, net of income tax expense of $501 and $0	1,711	554
Amortization of pension and postretirement plans, net of income tax expense of $931 and $2,204	2,097	4,969
Total other comprehensive income	21,611	6,498
COMPREHENSIVE INCOME	62,954	154,233
Less: Comprehensive income attributable to noncontrolling interest	5,425	—
COMPREHENSIVE INCOME ATTRIBUTABLE TO RAYONIER INC.	$57,529	$154,233
EARNINGS PER COMMON SHARE (Note 4)		
BASIC EARNINGS PER SHARE ATTRIBUTABLE TO RAYONIER INC.		
Continuing Operations	$0.33	$0.83
Discontinued Operations	—	0.36
Net Income	$0.33	$1.19
DILUTED EARNINGS PER SHARE ATTRIBUTABLE TO RAYONIER INC.		
Continuing Operations	$0.32	$0.79
Discontinued Operations	—	0.34
Net Income	$0.32	$1.13

See Notes to Consolidated Financial Statements.

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RAYONIER INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(Unaudited)
(Dollars in thousands)

	March 31, 2014	December 31, 2013
	(Restated)	
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	$156,071	$199,644
Accounts receivable, less allowance for doubtful accounts of $777 and $673	111,697	94,956
Inventory		
Finished goods	124,075	115,270
Work in progress	2,533	3,555
Raw materials	12,943	17,661
Manufacturing and maintenance supplies	2,377	2,332
Total inventory	141,928	138,818
Deferred tax assets	31,580	39,100
Prepaid and other current assets	54,577	46,576
Total current assets	495,853	519,094
TIMBER AND TIMBERLANDS, NET OF DEPLETION AND AMORTIZATION	2,067,549	2,049,378
PROPERTY, PLANT AND EQUIPMENT		
Land	20,620	20,138
Buildings	188,913	180,573
Machinery and equipment	1,756,924	1,760,641
Construction in progress	32,560	19,795
Total property, plant and equipment, gross	1,999,017	1,981,147
Less — accumulated depreciation	(1,137,048)	(1,120,326)
Total property, plant and equipment, net	861,969	860,821
OTHER ASSETS	217,458	256,208
TOTAL ASSETS	$3,642,829	$3,685,501
LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES		
Accounts payable	$86,282	$69,293
Current maturities of long-term debt	114,319	112,500
Accrued taxes	11,374	8,551
Accrued payroll and benefits	19,261	24,948
Accrued interest	13,857	9,531
Accrued customer incentives	10,082	9,580
Other current liabilities	35,870	34,874
Current liabilities for dispositions and discontinued operations (Note 13)	6,446	6,835
Total current liabilities	297,491	276,112
LONG-TERM DEBT	1,393,887	1,461,724
NON-CURRENT LIABILITIES FOR DISPOSITIONS AND DISCONTINUED OPERATIONS (Note 13)	67,456	69,543
PENSION AND OTHER POSTRETIREMENT BENEFITS (Note 15)	95,098	95,654
OTHER NON-CURRENT LIABILITIES	31,254	27,225
COMMITMENTS AND CONTINGENCIES (Notes 12 and 14)		

SHAREHOLDERS' EQUITY		
Common Shares, 480,000,000 shares authorized, 126,451,505 and 126,257,870 shares issued and outstanding	694,236	692,100
Retained earnings	994,624	1,015,209
Accumulated other comprehensive loss	(30,037)	(46,139)
TOTAL RAYONIER INC. SHAREHOLDERS' EQUITY	1,658,823	1,661,170
Noncontrolling interest	98,820	94,073
TOTAL SHAREHOLDERS' EQUITY	1,757,643	1,755,243
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$3,642,829	$3,685,501

See Notes to Consolidated Financial Statements.

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RAYONIER INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)
(Dollars in thousands)

	Three Months Ended March 31,	
	2014 (Restated)	2013
OPERATING ACTIVITIES		
Net income	$41,343	$147,735
Adjustments to reconcile net income to cash provided by operating activities:		
Depreciation, depletion and amortization	48,728	35,992
Non-cash cost of real estate sold	978	633
Stock-based incentive compensation expense	3,103	3,280
Deferred income taxes	5,596	1,832
Tax benefit of AFMC for CBPC exchange	—	(18,761)
Amortization of losses from pension and postretirement plans	3,028	6,279
Gain on sale of discontinued operations, net	—	(42,670)
Gain on foreign currency forward contracts	—	(1,881)
Other	(287)	(4,656)
Changes in operating assets and liabilities:		
Receivables	(15,950)	(8,778)
Inventories	(950)	11,197
Accounts payable	13,929	15,386
Income tax receivable/payable	1,319	15,915
All other operating activities	935	99
Payment to exchange AFMC for CBPC	—	(70,311)
Expenditures for dispositions and discontinued operations	(2,498)	(1,631)
CASH PROVIDED BY OPERATING ACTIVITIES	99,274	89,660
INVESTING ACTIVITIES		
Capital expenditures	(36,755)	(32,664)
Purchase of timberlands	(10,637)	(1,560)
Jesup mill cellulose specialties expansion (gross purchases of $0 and $57,693, net of purchases on account of $0 and $20,959)	—	(36,734)
Proceeds from disposition of Wood Products business	—	83,741
Change in restricted cash	45,312	9,908
Other	1,592	1,790
CASH (USED FOR) PROVIDED BY INVESTING ACTIVITIES	(488)	24,481
FINANCING ACTIVITIES		
Issuance of debt	31,819	100,000
Repayment of debt	(110,000)	(170,000)
Dividends paid	(62,545)	(57,744)
Proceeds from the issuance of common shares	2,027	4,091
Excess tax (deficiencies) benefits on stock-based compensation	(1,240)	6,191
Repurchase of common shares	(1,754)	(11,241)
Other	(679)	—
CASH USED FOR FINANCING ACTIVITIES	(142,372)	(128,703)
EFFECT OF EXCHANGE RATE CHANGES ON CASH	13	(17)
CASH AND CASH EQUIVALENTS		
Change in cash and cash equivalents	(43,573)	(14,579)

Balance, beginning of year	199,644	280,596
Balance, end of period	$156,071	$266,017
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION		
Cash paid during the period:		
Interest	$8,990	$3,562
Income taxes	$7,134	$70,403
Non-cash investing activity:		
Capital assets purchased on account	$17,891	$49,094

See Notes to Consolidated Financial Statements.

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RAYONIER INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
(Dollar amounts in thousands unless otherwise stated)

1. BASIS OF PRESENTATION

Basis of Presentation

The unaudited consolidated financial statements and notes thereto of Rayonier Inc. and its subsidiaries (“Rayonier” or the “Company”) have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and in accordance with the rules and regulations of the Securities and Exchange Commission (“SEC”). In the opinion of management, these financial statements and notes reflect all adjustments (all of which are normal recurring adjustments) necessary for a fair presentation of the results of operations, financial position and cash flows for the periods presented. These statements and notes should be read in conjunction with the financial statements and supplementary data included in the Company’s Annual Report on Form 10-K for the fiscal year ended December 31, 2013, as amended by Amendment No. 1 to the Form 10-K on Form 10-K/A (the “Amended Form 10-K”), as filed with the SEC.

Reclassifications

Certain 2013 amounts have been reclassified to agree with the current year presentation.

New Accounting Standards

In March 2013, the FASB issued Accounting Standards Update (“ASU”) No. 2013-05, Parent’s Accounting for the Cumulative Translation Adjustment upon Derecognition of Certain Subsidiaries or Groups of Assets within a Foreign Entity or of an Investment in a Foreign Entity. This standard requires a parent entity to release a related foreign entity’s cumulative translation adjustment into net income only if its sale or transfer results in the complete or substantially complete liquidation of the foreign entity in which the subsidiary or group of assets had resided. The cumulative translation adjustment should be released into net income if the transaction results in the loss of a controlling financial interest in a foreign entity or results in an acquirer obtaining control of an acquiree in which it held an equity interest immediately before the acquisition date. ASU No. 2013-05 became effective first quarter 2014. The adoption of this standard did not have any impact on the consolidated financial statements.

In July 2013, the FASB issued ASU No. 2013-11, Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists. The standard requires an unrecognized tax benefit to be presented in the financial statements as a reduction to a deferred tax asset for a net operating loss (“NOL”) or similar carryforward or a tax credit carryforward. If an NOL or tax credit carryforward is not available at the reporting date or tax law of the applicable jurisdiction does not require the entity to use the deferred tax asset for such purpose, the unrecognized tax benefit should be presented in the financial statements as a liability. ASU 2013-11 became effective first quarter of 2014. The Company has applied the standard to its income tax balances and it did not have a material impact on the Company’s financial position. See Note 5 — Income Taxes for further information.

Subsequent Events

The Company evaluated events and transactions that occurred after the balance sheet date but before financial statements were issued, and no subsequent events were identified that warranted disclosure.

Separation of Performance Fibers Business

In January 2014, the Company announced its intention to separate the Performance Fibers business from the Forest Resources and Real Estate businesses. The separation will result in two independent, publicly-traded companies by means of a tax-free spin-off to Rayonier shareholders of a newly formed company named Rayonier Advanced Materials Inc. which will contain the Performance Fibers segment of Rayonier. The separation, which is subject to a number of conditions including final Board approval, receipt of a favorable private letter ruling from the Internal Revenue Service (“IRS”) and effectiveness of a registration statement on Form 10, is expected to be completed by mid-2014.

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RAYONIER INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Unaudited)
(Dollar amounts in thousands unless otherwise stated)

2. SALE OF WOOD PRODUCTS BUSINESS

On March 1, 2013, Rayonier completed the sale of its Wood Products business (consisting of three lumber mills in Baxley, Swainsboro and Eatonton, Georgia) to International Forest Products Limited ("Interfor") for $80 million plus a working capital adjustment. Accordingly, the operating results of the Wood Products business, formerly reported as a separate operating segment, are classified as discontinued operations in the Company's Consolidated Statements of Income and Comprehensive Income for the three months ended March 31, 2013.

Rayonier recognized an after-tax gain of $42.7 million on the sale. The gain is included in "Income from discontinued operations, net" on the Consolidated Statements of Income and Comprehensive Income for the three months ended March 31, 2013.

The following table summarizes the operating results of the Company's discontinued operations and the related gain for the three months ended March 31, 2013, as presented in "Income from discontinued operations, net" on the Consolidated Statements of Income and Comprehensive Income:

	Three Months Ended March 31, 2013
Sales	$16,968
Income from discontinued operations, net	$44,477

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RAYONIER INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Unaudited)
(Dollar amounts in thousands unless otherwise stated)

3. RESTATEMENT OF PREVIOUSLY ISSUED CONSOLIDATED FINANCIAL STATEMENTS

Subsequent to the issuance of the Original Filing, the Company identified issues related to its historical timber harvest levels, its estimate of merchantable timber inventory and the effect of such estimate on its calculation of depletion expense in the quarterly period ended March 31, 2014. The Company determined that it had understated its depletion expense in cost of goods sold (referred to as "Cost of sales" in the Company's consolidated statements of income and comprehensive income) by approximately $2 million for the period. As a result, the financial amounts noted below have been restated from amounts previously reported.

The following tables summarize the effect of these restatements for the period:

	Consolidated Statements of Income and Comprehensive Income for the Three Months Ended March 31, 2014		
	As Previously Reported	Restatement	As Restated
Operating Income	$65,008	$(1,969)	$63,039
Income Tax Expense	(7,732)	20	(7,712)
Income from Continuing Operations	43,292	(1,949)	41,343
Net Income	43,292	(1,949)	41,343
Net Income Attributable to Rayonier Inc.	43,375	(1,949)	41,426
Basic Earnings Per Share Attributable to Rayonier Inc.			
Continuing Operations	$0.34	(0.01)	$0.33
Discontinued Operations	—	—	—
Net Income	$0.34	$(0.01)	$0.33
Diluted Earnings Per Share Attributable to Rayonier Inc.			
Continuing Operations	$0.34	(0.02)	$0.32
Discontinued Operations	—	—	—
Net Income	$0.34	$(0.02)	$0.32

	Consolidated Balance Sheet as of March 31, 2014		
	As Previously Reported	Restatement	As Restated
Prepaid and Other Current Assets	$54,557	$20	$54,577
Timber and Timberlands, Net of Depletion and Amortization	2,069,518	(1,969)	2,067,549
Retained earnings	996,573	(1,949)	994,624

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RAYONIER INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Unaudited)
(Dollar amounts in thousands unless otherwise stated)

4. EARNINGS PER COMMON SHARE

The following table provides details of the calculations of basic and diluted earnings per common share:

	Three Months Ended March 31,	
	2014	2013
	(Restated)	
Income from continuing operations	$41,343	$103,258
Less: Loss from continuing operations attributable to noncontrolling interest	(83)	—
Income from continuing operations attributable to Rayonier Inc.	$41,426	$103,258
Income from discontinued operations attributable to Rayonier Inc.	$—	$44,477
Net income attributable to Rayonier Inc.	$41,426	$147,735
Shares used for determining basic earnings per common share	126,344,987	124,479,865
Dilutive effect of:		
Stock options	286,535	533,031
Performance and restricted shares	83,850	448,440
Assumed conversion of Senior Exchangeable Notes (a)	1,063,538	2,115,959
Assumed conversion of warrants (a) (b)	645,583	2,859,593
Shares used for determining diluted earnings per common share	128,424,493	130,436,888
Basic earnings per common share attributable to Rayonier Inc.:		
Continuing operations	$0.33	$0.83
Discontinued operations	—	0.36
Net income	$0.33	$1.19
Diluted earnings per common share attributable to Rayonier Inc.:		
Continuing operations	$0.32	$0.79
Discontinued operations	—	0.34
Net income	$0.32	$1.13

	Three Months Ended March 31,	
	2014	2013
Anti-dilutive shares excluded from the computations of diluted earnings per share:		
Stock options, performance and restricted shares	731,046	220,701
Assumed conversion of exchangeable note hedges (a)	1,063,538	2,115,959
Total	1,794,584	2,336,660

(a) Rayonier will not issue additional shares upon future exchange or maturity of the Senior Exchangeable Notes due 2015 (the “2015 Notes”) due to offsetting hedges. Accounting Standards Codification 260, Earnings Per Share requires the assumed conversion of the 2015 Notes to be included in dilutive shares if the average stock price for the period exceeds the strike prices, while the assumed conversion of the hedges is excluded since they are anti-dilutive. As such, the full dilutive effect of the 2015 Notes was included for the three months ended March 31, 2013 and March 31, 2014.

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RAYONIER INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Unaudited)
(Dollar amounts in thousands unless otherwise stated)

The Senior Exchangeable Notes due 2012 (the “2012 Notes”) matured in October 2012; however, no additional shares were issued due to offsetting exchangeable note hedges. The warrants sold in conjunction with the 2012 Notes began maturing on January 15, 2013 and matured ratably through March 27, 2013. As a result, 2,037,303 shares were issued through the end of the first quarter of 2013. The dilutive impact of these warrants was calculated based on the length of time they were outstanding before settlement. Rayonier will distribute additional shares upon maturity of the warrants associated with the 2015 Notes if the stock price exceeds $38.97 per share. For further information, see Note 13 — Debt in the Amended Form 10-K and Note 16 — Debt of this Form 10-Q/A.

(b) The shares used for the assumed conversion of the warrants decreased in the first quarter of 2014 as there was no dilutive impact from the warrants on the 2012 Notes.

5. INCOME TAXES

Rayonier is a real estate investment trust (“REIT”). In general, only its taxable REIT subsidiaries, whose businesses include the Company’s non-REIT qualified activities, and foreign activities, are subject to corporate income taxes. Accordingly, the provision for corporate income taxes relates principally to current and deferred taxes on taxable REIT subsidiaries’ income and foreign operations.

Alternative Fuel Mixture Credit (“AFMC”) and Cellulosic Biofuel Producer Credit (“CBPC”)

The U.S. Internal Revenue Code allowed two credits for taxpayers that produced and used an alternative fuel in the operation of their business through December 31, 2009. The AFMC is a $.50 per gallon refundable tax credit (which is not taxable), while the CBPC is a $1.01 per gallon credit that is nonrefundable, taxable and has limitations based on an entity’s tax liability. Rayonier produces and uses an alternative fuel (“black liquor”) at its Jesup, Georgia and Fernandina Beach, Florida Performance Fibers mills, which qualified for both credits. The Company claimed the AFMC on its original 2009 tax return. In the first quarter of 2013, management approved a $70 million tax payment to exchange approximately 120 million gallons of black liquor previously claimed for the AFMC for the CBPC, resulting in a $19 million tax benefit.

Provision for Income Taxes from Continuing Operations

The Company’s effective tax rate is below the 35 percent U.S. statutory tax rate primarily due to tax benefits associated with being a REIT. The Company’s effective tax rate in the prior year period was lower than 2014 primarily due to recording the above referenced AFMC exchange. Excluding the AFMC for CBPC exchange, the effective tax rate decreased in the first quarter 2014 compared to the prior year period principally due to proportionately higher earnings from REIT operations.

The table below reconciles the U.S. statutory rate to the Company’s effective tax rate for each period presented (in millions of dollars):

	Three Months Ended March 31,			
	2014		2013	
	(Restated)	(Restated)		
Income tax expense at federal statutory rate	$17	35.0 %	$38	35.0 %
REIT income not subject to tax	(7)	(14.2)	(11)	(10.1)
Manufacturing deduction	(1)	(2.2)	(2)	(2.2)
Other	—	(0.1)	—	0.7
Income tax expense before discrete items	9	18.5 %	25	23.4 %
Exchange of AFMC for CBPC	—	—	(19)	(17.5)
Other	(1)	(2.8)	(2)	(1.8)
Income tax expense as reported	$8	15.7 %	$4	4.1 %

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RAYONIER INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Unaudited)
(Dollar amounts in thousands unless otherwise stated)

Provision for Income Taxes from Discontinued Operations

In first quarter 2013, Rayonier completed the sale of its Wood Products business for $80 million plus a working capital adjustment. For the three months ended March 31, 2013, income tax expense related to discontinued operations was $22.3 million ($21.4 million from the gain on sale). See Note 2 — Sale of Wood Products Business for additional information.

Unrecognized Tax Benefits

During the first quarter of 2013, the Company implemented ASU 2013-11, which requires, in certain instances, an unrecognized tax benefit (or portion of an unrecognized tax benefit) to be presented in the financial statements as a reduction to a deferred tax asset for a net operating loss carryforward, a similar tax loss or a tax credit carryforward. As a result, the Company reclassified $3.9 million from an unrecognized tax benefit liability to a reduction to current deferred tax assets at March 31, 2014.

6. RESTRICTED DEPOSITS

In order to qualify for like-kind exchange ("LKE") treatment, the proceeds from real estate sales must be deposited with a third-party intermediary. These proceeds are accounted for as restricted cash until a suitable replacement property is acquired. In the event LKE purchases are not completed, the proceeds are returned to the Company after 180 days and reclassified as available cash. As of March 31, 2014 and December 31, 2013, the Company had $23.6 million and $68.9 million, respectively, of proceeds from real estate sales classified as restricted cash in Other Assets, which were deposited with an LKE intermediary.

7. JOINT VENTURE INVESTMENT

On April 4, 2013 (the "acquisition date"), the Company acquired an additional 39 percent ownership interest in Matariki Forestry Group, a joint venture ("New Zealand JV") that owns or leases approximately 0.3 million acres of New Zealand timberlands. As a result of the acquisition, Rayonier is a 65 percent owner of the New Zealand JV and 100 percent of the results of its operations subsequent to April 4, 2013 have been included in the Company's consolidated financial statements, along with 100 percent of the JV's assets and liabilities at March 31, 2014 and December 31, 2013. The portions of the consolidated financial position and results of operations attributable to the New Zealand JV's 35 percent noncontrolling interest are also shown separately. Rayonier New Zealand Limited ("RNZ"), a wholly-owned subsidiary of Rayonier Inc., continues to serve as the manager of the New Zealand JV forests.

Prior to the acquisition date, the Company accounted for its 26 percent interest in the New Zealand JV as an equity method investment. The additional 39 percent interest was acquired for $139.9 million and resulted in the Company obtaining a controlling financial interest in the New Zealand JV and accordingly, the purchase was accounted for as a step-acquisition. Upon consolidation, the Company recognized a $10.1 million deferred gain, which resulted from the original sale of its New Zealand operations to the joint venture in 2005 and a $6 million benefit due to the required fair market value remeasurement of the Company's equity interest in the New Zealand JV held before the purchase of the additional interest. The acquisition-date fair value of the previous equity interest was $93.3 million.

We have applied estimates and judgments in order to determine the fair value of assets acquired and liabilities assumed at the acquisition date. In determining fair value we utilized valuation methodologies including discounted cash flow analysis. The assumptions made in performing these valuations include assumptions as to discount rates, foreign exchange rates, and commodity prices.

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The Company’s operating results for the three months ended March 31, 2013 reflect 26 percent of the New Zealand JV’s income prior to the acquisition date, as reported in “Equity in income of New Zealand joint venture” in the Consolidated Statements of Income and Comprehensive Income. The amounts of revenue and earnings of the New Zealand JV included in the Company’s Consolidated Statements of Income and Comprehensive Income for the first quarter 2014 are as follows:

	Three Months Ended March 31, 2014
Sales	$37,764
Net Loss	(734)

The following represents the pro forma Rayonier consolidated sales and net income for the three months ended March 31, 2013 as if the additional interest in the New Zealand JV had been acquired on January 1, 2012.

	Three Months Ended March 31, 2013
Sales	$428,245
Net Income	$146,280

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8. SHAREHOLDERS' EQUITY

An analysis of shareholders' equity for the three months ended March 31, 2014 and the year ended December 31, 2013 is shown below (share amounts not in thousands):

	Rayonier Inc. Shareholders Equity					
	Common Shares					
	Shares	Amount	Retained Earnings (Restated)	Accumulated Other Comprehensive Income/(Loss)	Non-controlling Interest	Total Shareholders' Equity (Restated)
Balance, December 31, 2012	123,332,444	$670,749	$876,634	$(109,379)	$ —	$1,438,004
Net income	—	—	371,896	—	1,902	373,798
Dividends ($1.86 per share)	—	—	(233,321)	—	—	(233,321)
Issuance of shares under incentive stock plans	1,001,426	10,101	—	—	—	10,101
Stock-based compensation	—	11,710	—	—	—	11,710
Excess tax benefit on stock-based compensation	—	8,413	—	—	—	8,413
Repurchase of common shares	(211,221)	(11,326)	—	—	—	(11,326)
Equity portion of convertible debt (Note 15)	—	2,453	—	—	—	2,453
Settlement of warrants (Note 15)	2,135,221	—	—	—	—	—
Net gain from pension and postretirement plans	—	—	—	61,869	—	61,869
Acquisition of noncontrolling interest	—	—	—	—	96,336	96,336
Noncontrolling interest redemption of shares	—	—	—	—	(713)	(713)
Foreign currency translation adjustment	—	—	—	(1,915)	(3,795)	(5,710)
Joint venture cash flow hedges	—	—	—	3,286	343	3,629
Balance, December 31, 2013	126,257,870	$692,100	$1,015,209	$(46,139)	$ 94,073	$1,755,243
Net income (loss)	—	—	41,426	—	(83)	41,343
Dividends ($0.49 per share)	—	—	(62,011)	—	—	(62,011)
Issuance of shares under incentive stock plans	235,843	2,027	—	—	—	2,027
Stock-based compensation	—	3,103	—	—	—	3,103
Excess tax deficiency on stock-based compensation	—	(1,240)	—	—	—	(1,240)
Repurchase of common shares	(42,208)	(1,754)	—	—	—	(1,754)
Amortization of pension and postretirement plans	—	—	—	2,097	—	2,097
Noncontrolling interest redemption of shares	—	—	—	—	(679)	(679)
Foreign currency translation adjustment	—	—	—	12,893	4,910	17,803

Joint venture cash flow hedges	—	—	—	1,112	599	1,711
Balance, March 31, 2014	126,451,505	$694,236	$994,624	$(30,037)	$ 98,820	$1,757,643

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9. SEGMENT AND GEOGRAPHICAL INFORMATION

Rayonier operates in three reportable business segments: Forest Resources, Real Estate and Performance Fibers. Forest Resources sales include all activities related to the harvesting of timber. Real Estate sales include all property sales, including those designated for higher and better use ("HBU"). The assets of the Real Estate segment include HBU property held by the Company's real estate subsidiary, TerraPointe LLC. The Performance Fibers segment includes two major product lines, cellulose specialties and commodity grade products (primarily viscose). The Company's remaining operations include harvesting and selling timber acquired from third parties (log trading). These operations are reported in "Other Operations." Sales between operating segments are made based on estimated fair market value, and intercompany sales, purchases and profits (losses) are eliminated in consolidation. The Company evaluates financial performance based on the operating income of the segments.

Operating income (loss) as presented in the Consolidated Statements of Income and Comprehensive Income is equal to segment income (loss). Certain income (loss) items in the Consolidated Statements of Income and Comprehensive Income are not allocated to segments. These items, which include gains (losses) from certain asset dispositions, interest income (expense), miscellaneous income (expense) and income tax (expense) benefit, are not considered by management to be part of segment operations.

Total assets, sales, operating income (loss) and depreciation, depletion and amortization by segment including Corporate were as follows:

ASSETS	March 31, 2014 (Restated)	December 31, 2013
Forest Resources	$2,187,498	$2,162,913
Real Estate	113,376	149,001
Performance Fibers	1,095,574	1,078,645
Other Operations	35,121	37,334
Corporate and other	211,260	257,608
Total	$3,642,829	$3,685,501

	Three Months Ended March 31,	
SALES	2014	2013
Forest Resources (a)	$104,678	$57,102
Real Estate	5,530	24,297
Performance Fibers	241,768	284,188
Other Operations	37,417	28,227
Intersegment Eliminations	(2,707)	(95)
Total	$386,686	$393,719

(a) First quarter 2014 included $38 million in sales from the consolidation of the New Zealand JV. See Note 7 — Joint Venture Investment.

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	Three Months Ended March 31,	
	2014	2013
OPERATING INCOME	(Restated)	
Forest Resources	$25,546	$13,255
Real Estate	725	16,842
Performance Fibers	48,980	91,670
Other Operations	184	165
Corporate and other (a)	(12,396)	(6,569)
Total	$63,039	$115,363

(a) First quarter 2014 included $3.3 million of separation costs related to the planned separation of the Performance Fibers business from the Forest Resources and Real Estate businesses.

	Three Months Ended March 31,	
	2014	2013
DEPRECIATION, DEPLETION AND AMORTIZATION	(Restated)	
Forest Resources (a)	26,887	$16,444
Real Estate	910	4,177
Performance Fibers	20,649	15,153
Corporate and other	282	218
Total	$48,728	$35,992

(a) 2014 included an increase of approximately $7 million in depletion expenses related to the consolidation of the New Zealand JV. See Note 7 — Joint Venture Investment.

10. DERIVATIVE FINANCIAL INSTRUMENTS AND HEDGING ACTIVITIES

The Company is exposed to market risk related to potential fluctuations in foreign currency exchange rates, interest rates and fuel prices. The Company’s New Zealand JV uses derivative financial instruments to mitigate the financial impact of exposure to these risks.

Accounting for derivative financial instruments is governed by Accounting Standards Codification Topic 815, Derivatives and Hedging, (“ASC 815”). In accordance with ASC 815, the Company records its derivative instruments at fair value as either assets or liabilities in the Consolidated Balance Sheets. Changes in the instruments’ fair value are accounted for based on their intended use. Gains and losses on derivatives that are designated and qualify for cash flow hedge accounting are recorded as a component of accumulated other comprehensive income (“AOCI”) and reclassified into earnings when the hedged transaction materializes. The ineffective portion of any hedge as well as changes in the fair value of derivatives not designated as hedging instruments and those which are no longer effective as hedging instruments, are recognized immediately in earnings.

Foreign Currency Exchange and Option Contracts

The functional currency of the New Zealand JV is the New Zealand dollar. These operations are exposed to foreign currency risk on export sales and ocean freight payments which are predominately denominated in US dollars. The New Zealand JV typically hedges at least 70 percent of its estimated foreign currency exposure with respect to the following three months forecasted sales and purchases and 50 percent of the forward twelve months.

The fair value of foreign currency exchange contracts is determined by a mark-to-market valuation which estimates fair value by discounting the difference between the contracted forward price and the current forward price for the residual maturity of the contract using a risk-free interest rate. The fair value of foreign currency option contracts is based on a mark-to-market calculation using the Black Scholes option pricing model.

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Interest Rate Swaps
The Company uses interest rate swaps to manage the New Zealand JV's exposure to interest rate movements on its variable rate debt attributable to changes in the New Zealand Bank bill rate. By converting a portion of these borrowings from floating rates to fixed rates the Company has reduced the impact of interest rate changes on its expected future cash outflows. As of March 31, 2014, the Company's interest rate contracts hedged 88 percent of the New Zealand JV's variable rate debt and had maturity dates through January 2020.
Fuel Hedge Contracts
The Company uses fuel swap contracts to manage its New Zealand JV's exposure to changes in New Zealand's domestic diesel prices. The fuel swaps are quoted by domestic banks in New Zealand dollar price terms. As of March 31, 2014 all of the contracts had maturities of less than one year. The fair value of the fuel swap contracts is determined by a mark-to-market valuation which estimates fair value by discounting the difference between the contracted forward price and the current forward price for the residual maturity of the contract.
The following table demonstrates the impact of the Company's derivatives on the Consolidated Statements of Income and Comprehensive Income for the three months ended March 31, 2014. No derivative balances were consolidated prior to the Company's acquisition of a controlling interest in the New Zealand JV in the second quarter of 2013.

	Income Statement Location	Three Months Ended March 31, 2014
Derivatives designated as cash flow hedges:		
Foreign currency exchange contracts	Other comprehensive income (loss)	$1,487
Foreign currency option contracts	Other comprehensive income (loss)	725
Derivatives not designated as hedging instruments:		
Foreign currency exchange contracts	Other operating expense (income)	25
Foreign currency option contracts	Other operating expense (income)	7
Interest rate swaps	Interest and miscellaneous (expense) income, net	(1,134)
Fuel hedge contracts	Cost of sales	317

During the next 12 months, the amount of the March 31, 2014 AOCI balance, net of tax, expected to be reclassified into earnings as a result of the maturation of the Company's derivative instruments is a gain of approximately $2.7 million.
The following table contains the notional amounts of the derivative financial instruments recorded in the Consolidated Balance Sheets:

	Notional Amount (a)	
	March 31, 2014	December 31, 2013
Derivatives designated as cash flow hedges:		
Foreign currency exchange contracts	$37,064	$32,300
Foreign currency option contracts	37,500	38,000
Derivatives not designated as hedging instruments:		
Foreign currency exchange contracts	$—	$1,950
Foreign currency option contracts	—	4,000
Interest rate swaps	179,066	183,851
Fuel hedge contracts	25	38

(a) All notional amounts are stated in thousands of dollars except fuel contracts which are denominated in thousands of barrels.

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The following table contains the fair values of the derivative financial instruments recorded in the Consolidated Balance Sheets :

	Location on Balance Sheet	Fair Value Assets (Liabilities) (a)	
		March 31, 2014	December 31, 2013
Derivatives designated as cash flow hedges:			
Foreign currency exchange contracts	Prepaid and other current assets	$2,616	$915
	Other current liabilities	(84)	—
Foreign currency option contracts	Prepaid and other current assets	1,333	673
	Other current liabilities	(90)	(214)
Derivatives not designated as hedging instruments:			
Foreign currency exchange contracts	Prepaid and other current assets	$—	$25
Foreign currency option contracts	Prepaid and other current assets	—	8
Interest rate swaps	Other non-current liabilities	(5,145)	(4,659)
Fuel hedge contracts	Prepaid and other current assets	—	160
	Other current liabilities	(159)	—
Total derivative contracts:			
Prepaid and other current assets		$3,949	$1,781
Other current liabilities		(333)	(214)
Other non-current liabilities		(5,145)	(4,659)
Total derivative liabilities		$(5,478)	$(4,873)

(a) See Note 11 — Fair Value Measurements for further information on the fair value of our derivatives including their classification within the fair value hierarchy.

Offsetting Derivatives

Derivative financial instruments are presented at their gross fair values in the Consolidated Balance Sheets. The Company’s derivative financial instruments are not subject to master netting arrangements which would allow the right of offset.

11. FAIR VALUE MEASUREMENTS

Fair Value of Financial Instruments

The Accounting Standards Codification established a three-level hierarchy that prioritizes the inputs used to measure fair value as follows:

Level 1 — Quoted prices in active markets for identical assets or liabilities.
Level 2 — Observable inputs other than quoted prices included in Level 1.
Level 3 — Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

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The following table presents the carrying amount, estimated fair values and categorization under the fair value hierarchy of financial instruments held by the Company at March 31, 2014 and December 31, 2013, using market information and what management believes to be appropriate valuation methodologies under generally accepted accounting principles:

	March 31, 2014			December 31, 2013		
Asset (liability)	Carrying Amount	Fair Value		Carrying Amount	Fair Value	
		Level 1	Level 2		Level 1	Level 2
Cash and cash equivalents	$156,071	$156,071	$—	$199,644	$199,644	$—
Restricted cash (a)	23,633	23,633	—	68,944	68,944	—
Current maturities of long-term debt	(114,319)	—	(122,187)	(112,500)	—	(119,614)
Long-term debt	(1,393,887)	—	(1,451,984)	(1,461,724)	—	(1,489,810)
Interest rate swaps (b)	(5,145)	—	(5,145)	(4,659)	—	(4,659)
Foreign currency exchange contracts (b)	2,532	—	2,532	940	—	940
Foreign currency option contracts (b)	1,243	—	1,243	467	—	467
Fuel contracts (b)	(159)	—	(159)	160	—	160

(a) Restricted cash is recorded in “Other Assets” and represents the proceeds from LKE sales deposited with a third-party intermediary.
(b) See Note 10 — Derivative Financial Instruments and Hedging Activities for information regarding the Balance Sheet classification of the Company’s derivative financial instruments.

Rayonier uses the following methods and assumptions in estimating the fair value of its financial instruments:
Cash and cash equivalents and Restricted cash — The carrying amount is equal to fair market value.
Debt — The fair value of fixed rate debt is based upon quoted market prices for debt with similar terms and maturities. The variable rate debt adjusts with changes in the market rate, therefore the carrying value approximates fair value.
Interest rate swap agreements — The fair value of interest rate contracts is determined by discounting the expected future cash flows, for each instrument, at prevailing interest rates.
Foreign currency exchange contracts — The fair value of foreign currency exchange contracts is determined by a mark-to-market valuation which estimates fair value by discounting the difference between the contracted forward price and the current forward price for the residual maturity of the contract using a risk-free interest rate.
Foreign currency option contracts — The fair value of foreign currency option contracts is based on a mark-to-market calculation using the Black-Scholes option pricing model.

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12. GUARANTEES

The Company provides financial guarantees as required by creditors, insurance programs, and various governmental agencies. As of March 31, 2014, the following financial guarantees were outstanding:

Financial Commitments	Maximum Potential Payment	Carrying Amount of Associated Liability
Standby letters of credit (a)	$17,355	$15,000
Guarantees (b)	2,254	43
Surety bonds (c)	5,498	1,099
Total financial commitments	$25,107	$16,142

(a) Approximately $15 million of the standby letters of credit serve as credit support for industrial revenue bonds. The remaining letters of credit support various insurance related agreements, primarily workers' compensation and pollution liability policy requirements. These letters of credit will expire at various dates during 2014 and will be renewed as required.

(b) In conjunction with a timberland sale and note monetization in the first quarter of 2004, the Company issued a make-whole agreement pursuant to which it guaranteed $2.3 million of obligations of a special-purpose entity that was established to complete the monetization. At March 31, 2014, the Company has a de minimus liability to reflect the fair market value of its obligation to perform under the make-whole agreement.

(c) Rayonier issues surety bonds primarily to secure timber harvesting obligations in the State of Washington and to provide collateral for the Company's workers' compensation self-insurance program in that state. These surety bonds expire at various dates during 2014 and 2015 and are expected to be renewed as required.

13. LIABILITIES FOR DISPOSITIONS AND DISCONTINUED OPERATIONS

An analysis of the liabilities for dispositions and discontinued operations follows:

	March 31, 2014	December 31, 2013
Balance, beginning of period	$76,378	$81,695
Expenditures charged to liabilities	(2,498)	(8,570)
Increase to liabilities	22	3,253
Balance, end of period	73,902	76,378
Less: Current portion	(6,446)	(6,835)
Non-current portion	$67,456	$69,543

These prior dispositions and discontinued operations are exposed to the risk of reasonably possible additional losses in excess of the established liabilities. As of March 31, 2014, this amount could range up to $30 million, attributable to several of the applicable sites, and arises from uncertainty over the availability, feasibility and effectiveness of certain remediation technologies, additional or different contamination that may be discovered, development of new or more effective environmental remediation technologies, potential changes in applicable law and regulations, and the exercise of discretion in interpretation of applicable law and regulations by governmental agencies.

Management believes established liabilities are sufficient for probable costs expected to be incurred over the next 20 years with respect to its dispositions and discontinued operations. Remedial actions for these sites vary, but include on-site (and in certain cases off-site) removal or treatment of contaminated soils and sediments, recovery and treatment/remediation of groundwater, and source remediation and/or control.

14. CONTINGENCIES

Rayonier is engaged in various legal actions, including certain environmental proceedings, and has been named as a defendant in various other lawsuits and claims arising in the normal course of business. While the Company has procured reasonable and customary insurance covering risks normally occurring in connection with its businesses, it has in certain cases retained some risk through the operation of self-insurance, primarily in the areas of workers' compensation, property insurance and general liability. These other lawsuits and claims, either individually or in the aggregate, are not expected to have a material adverse effect on the Company's financial position, results of operations, or cash flow.

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15. EMPLOYEE BENEFIT PLANS

The Company has four qualified non-contributory defined benefit pension plans covering a significant majority of its employees and an unfunded plan that provides benefits in excess of amounts allowable under current tax law in the qualified plans. Currently, all qualified plans are closed to new participants. Employee benefit plan liabilities are calculated using actuarial estimates and management assumptions. These estimates are based on historical information, along with certain assumptions about future events. Changes in assumptions, as well as changes in actual experience, could cause the estimates to change.

The net pension and postretirement benefit costs that have been recorded are shown in the following tables:

	Pension Three Months Ended March 31,		Postretirement Three Months Ended March 31,	
	2014	2013	2014	2013
Components of Net Periodic Benefit Cost				
Service cost	$1,624	$2,419	$179	$249
Interest cost	4,683	4,834	206	240
Expected return on plan assets	(6,658)	(7,424)	—	—
Amortization of prior service cost	292	388	4	6
Amortization of losses	2,737	5,727	129	218
Amortization of negative plan amendment	—	—	(134)	—
Net periodic benefit cost	$2,678	$5,944	$384	$713

In 2014, the Company has no mandatory pension contribution requirements, but may make discretionary contributions.

16. DEBT

As of December 31, 2013, the 2015 Notes became exchangeable at the option of the holders for the calendar quarter ended March 31, 2014. According to the indenture, in order for the notes to become exchangeable, the Company’s stock price must exceed 130 percent of the exchange price for 20 trading days during a period of 30 consecutive trading days as of the last day of the quarter. During the quarter ended March 31, 2014, the note holders did not elect to exercise the exchange option. Based upon the average stock price for the 30 trading days ended March 31, 2014, these notes again became exchangeable at the option of the holder for the calendar quarter ending June 30, 2014. The entire balance of the notes is classified as long-term debt at March 31, 2014 due to the ability and intent of the Company to refinance them on a long-term basis.

During the three months ended March 31, 2014, the Company made net repayments of $80 million on its unsecured revolving credit facility. The Company had $323 million of available borrowings under this facility at March 31, 2014, net of $2 million to secure its outstanding letters of credit. During the three months ended March 31, 2014, the New Zealand JV borrowed $1.8 million on its working capital facility. Additional draws totaling $18.1 million remain available on the facility.

There were no other significant changes to the Company’s outstanding debt as reported in Note 13 — Debt in the Company’s Amended Form 10-K.

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17. ACCUMULATED OTHER COMPREHENSIVE LOSS
The following table summarizes the changes in AOCI by component for the three months ended March 31, 2014. All amounts are presented net of tax and exclude portions attributable to noncontrolling interest.

	Foreign currency translation gains	New Zealand joint venture cash flow hedges	Unrecognized components of employee benefit plans	Total
Balance as of December 31, 2013	$36,914	$(342)	$(82,711)	$(46,139)
Other comprehensive income before reclassifications	12,893	1,604	—	14,497
Amounts reclassified from accumulated other comprehensive income				