Notes to Financial Statements

> NOTE 1 Basis of Presentation

Financial statements for all periods presented herein have been prepared on a consolidated basis in accordance with generally accepted accounting principles consistently applied. All per-share information is presented on a diluted basis unless otherwise noted. Certain amounts in the prior years' financial statements have been reclassified to conform with the presentation used in 2002.

The company has three operating segments: Consumer and Foodservice/Food Packaging, which relates to the manufacture and sale of disposable plastic, molded-fibre, pressed-paperboard, and aluminum packaging products for the consumer, foodservice, and food-packaging markets; Protective and Flexible Packaging, which relates to the manufacture and sale of plastic, paperboard, and molded-fibre products for protective-packaging markets such as electronics, automotive, furniture, and e-commerce, and for flexible-packaging applications in food, medical, pharmaceutical, chemical, and hygienic markets; and Other, which relates to corporate and administrative service operations and retiree-benefit income and expense.

> NOTE 2 Summary of Accounting Policies

Consolidation

The financial statements of the company include all majority-owned subsidiaries. Investments in 20%- to 50%-owned companies in which Pactiv has the ability to exert significant influence over operating and financial policies are carried at cost plus share of equity in undistributed earnings since date of acquisition. All significant intercompany transactions are eliminated.

Foreign-Currency Translation

Financial statements of international operations are translated into U.S. dollars using end-of-period exchange rates for assets and liabilities and the periods' weighted-average exchange rates for sales, expenses, gains, and losses. Translation adjustments are recorded as a component of shareholders' equity.

Cash and Temporary Cash Investments

The company defines cash and temporary cash investments as checking accounts, money-market accounts, certificates of deposit, and U.S. Treasury notes having an original maturity of 90 days or less.

Accounts and Notes Receivable

Trade accounts receivable are classified as current assets and are reported net of allowances for doubtful accounts. The company records such allowances based on a number of factors, including historical trends and specific customer liquidity.

On a recurring basis, the company sells an undivided interest in a pool of trade receivables meeting certain criteria to a third party as an alternative to debt financing. Amounts sold were $10 million and $44 million at December 31, 2002, and 2001, respectively. Such sales, which represent a form of off-balance-sheet financing, are recorded as a reduction of accounts and notes receivable in the statement of financial position, and changes in such amounts are included in cash provided by operating activities in the statement of cash flows. Discounts and fees related to these sales totaled $1 million, $5 million, and $7 million in 2002, 2001, and 2000, respectively, and were included in other income/expense in the statement of income. In the event that either Pactiv or the third-party purchaser of the trade receivables were to discontinue this program, the company's debt would increase or its cash balance would decrease by an amount corresponding to the level of sold receivables at such time.

Inventories

Inventories are stated at the lower of cost or market. A portion of inventories (56% at December 31, 2002, and 2001) is valued using the last-in, first-out method of accounting. All other inventories are valued using the first-in, first-out (FIFO) or average-cost methods. If FIFO or average-cost methods had been used to value all inventories, the total inventory balance would have been $11 million lower at December 31, 2002, and $9 million lower at December 31, 2001.

Property, Plant, and Equipment, Net

Depreciation is recorded on a straight-line basis over the estimated useful lives of assets. Useful lives range from 10 to 40 years for buildings and improvements and from 3 to 25 years for machinery and equipment. Depreciation expense totaled $140 million, $145 million, and $150 million for the years ended December 31, 2002, 2001, and 2000, respectively.

The company capitalizes certain costs related to the purchase and development of software used in its business. Such costs are amortized over the estimated useful lives of the assets, ranging from 3 to 12 years. Capitalized software-development costs, net of amortization, were $57 million and $64 million at December 31, 2002, and 2001, respectively.

The company periodically re-evaluates carrying values and estimated useful lives of long-lived assets to determine if adjustments are warranted. The company uses estimates of undiscounted cash flows from long-lived assets to determine whether the book value of such assets is recoverable over the assets' remaining useful lives.

In 2001, the company changed estimated useful lives for certain assets of the Protective and Flexible Packaging business in North America and Europe to be consistent with those used for similar assets in its other business segment. This change did not have a material impact on the company's financial statements.

Goodwill and Intangibles, Net

Effective January 1, 2002, the company adopted Statement of Financial Accounting Standards (SFAS) No. 142, "Goodwill and Other Intangible Assets." SFAS No. 142 does not permit goodwill and indefinite-lived

intangibles to be amortized, but requires that these assets be reviewed at least annually for possible impairment. Capitalized intangible assets with definite lives are amortized on a straight-line basis over periods ranging from 5 to 26 years. See Note 9 for further information regarding goodwill and intangible assets.

Environmental Liabilities

Expenditures for compliance with environmental regulations that relate to ongoing operations are expensed or capitalized as appropriate. Expenditures for conditions that relate to operations that no longer contribute to the generation of sales are expensed as incurred or as warranted by environmental assessments. Liabilities are recorded when environmental assessments indicate that remedial efforts are probable and that costs can be reasonably estimated. Estimated liabilities are based on currently available facts, existing technology, and requirements of current laws and regulations, taking into consideration the likely effects of inflation and other factors. All available evidence is considered, including prior remediation experience with contaminated sites, other companies' clean-up experience, and data released by the U. S. Environmental Protection Agency or other organizations. Estimated liabilities are subject to revision in subsequent periods based on actual cost data or new information. Liabilities reflected in the statement of financial position are not discounted.

Sales Recognition

The company recognizes sales when the risks and rewards of ownership have transferred to the customer, which is generally considered to have occurred as products are shipped.

Freight

The company records amounts billed to customers for shipping and handling as sales, and records shipping and handling expenses as cost of sales.

General and Administrative Expenses

The company records net pension income as an offset to selling, general, and administrative expenses. Such noncash income totaled $109 million, $113 million, and $108 million in 2002, 2001, and 2000, respectively.

Research and Development

Research and development costs, which are expensed as incurred, totaled $35 million, $40 million, and $36 million in 2002, 2001, and 2000, respectively.

Advertising

Advertising production costs are expensed as incurred, while advertising media costs are expensed in the period in which the related advertising first takes place. Advertising expenses were $17 million, $11 million, and $3 million in 2002, 2001, and 2000, respectively.

Stock-Based Compensation

In accounting for stock-based employee compensation, the company uses the intrinsic-value method specified in Accounting Principles Board (APB) Opinion No. 25, "Accounting for Stock Issued to Employees." Shown below are net income and basic and diluted earnings per share as reported and adjusted to reflect the use of the fair-value method in determining stock-based compensation costs, as prescribed in SFAS No. 123, "Accounting for Stock-Based Compensation."

(In millions, except per-share data)	2002	2001	2000
Net income reported	$ 148	$ 193	$ 247
After-tax adjustment of stock-based compensation costs:			
Intrinsic-value method	4	2	2
Fair-value method	(13)	(11)	(12)
Pro forma	$ 139	$ 184	$ 237
Earnings per share			
Basic	$ 0.93	$ 1.21	$ 1.53
Adjustment of stock-based compensation costs:			
Intrinsic-value method	0.02	0.01	0.01
Fair-value method	(0.08)	(0.07)	(0.07)
Pro forma	$ 0.87	$ 1.15	$ 1.47
Diluted	$ 0.92	$ 1.20	$ 1.53
Adjustment of stock-based compensation costs:			
Intrinsic-value method	0.02	0.01	0.01
Fair-value method	(0.08)	(0.07)	(0.07)
Pro forma	$ 0.86	$ 1.14	$ 1.47

Income Taxes

The company utilizes the asset and liability method of accounting for income taxes, which requires that deferred tax assets and liabilities be recorded to reflect the future tax consequences of temporary timing differences between the tax and financial-statement basis of assets and liabilities. Deferred tax assets are reduced by a valuation allowance if management determines that it is more likely than not that a portion of deferred tax assets will not be realized in a future period. Estimates used to recognize deferred tax assets are subject to revision in subsequent periods based on new facts or circumstances.

The company does not provide for U.S. federal income taxes on unremitted earnings of foreign subsidiaries in that it is management's present intention to reinvest those earnings in foreign operations. Unremitted earnings of foreign subsidiaries totaled $110 million and $105 million at December 31, 2002, and December 31, 2001, respectively. The unrecognized deferred tax liability associated with these unremitted earnings totaled approximately $24 million at December 31, 2002.

Earnings Per Share

Basic earnings per share is computed by dividing income available to common shareholders by the weighted-average number of shares outstanding. Diluted earnings per share is calculated in the same manner; however, adjustments are made to reflect the potential issuance of dilutive shares.

Risk Management

From time to time, the company uses derivative financial instruments, principally foreign-currency purchase and sale contracts with terms less than 1 year, to hedge its exposure to changes in foreign-currency exchange rates. Net gains or losses on such contracts are recognized in the income statement as offsets to foreign-currency gains or losses on the underlying transactions. In the statement of cash flows, cash receipts and payments related to hedge contracts are classified in the same way as cash flows from the transactions being hedged.

Interest-rate risk management is accomplished through the use of swaps to create synthetic debt instruments. Gains and losses on the settlement of swaps are amortized over the remaining life of the underlying asset or liability. The company does not use derivative financial instruments for speculative purposes.

Changes in Accounting Principles

In May 2000, the Financial Accounting Standards Board's (FASB's) Emerging Issues Task Force (EITF) reached a consensus on Issue No. 00-14, "Accounting for Certain Sales Incentives." This issue addresses the recognition, measurement, and income-statement classification of various types of sales incentives, including discounts, coupons, rebates, and free products. With the company's fourth-quarter 2001 adoption of EITF No. 00-14, certain expenses that historically (i.e., 2001 and prior years) had been included in selling, general, and administrative costs were reclassified as deductions from sales for all periods presented herein.

In April 2001, the EITF reached a consensus on Issue No. 00-25, "Accounting for Consideration from a Vendor to a Retailer in Connection with the Purchase or Promotion of the Vendor's Products." This consensus requires that consideration provided by a vendor to a purchaser of its products be recognized as a reduction of sales, except in those instances where an identifiable and measurable benefit is or will be received by the vendor from the purchaser. With the company's fourth-quarter 2001 adoption of EITF No. 00-25, certain expenses that historically (i.e., 2001 and prior years) had been included in selling, general, and administrative costs were reclassified as deductions from sales for all periods presented herein.

In July 2001, the FASB issued SFAS No. 141, "Business Combinations," and SFAS No. 142. SFAS No. 141 requires that business combinations initiated after June 30, 2001, be accounted for using the purchase method of accounting and broadens the criteria for recording intangible assets separate from goodwill. SFAS No. 142 does not permit goodwill and certain intangibles to be amortized, but requires that an impairment loss be recognized if recorded amounts exceed fair values. Effective January 1, 2002, the company adopted SFAS No. 142, and recorded a goodwill-impairment charge of $83 million, $72 million after tax, or $0.45 per share, in the first quarter of 2002. Adoption of SFAS No. 142 added $19 million, $14 million, and $0.09 to income before interest, income taxes, and minority interest; net income from continuing operations; and earnings per share, respectively, for 2002.

In July 2002, the FASB issued SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities." SFAS No. 146 requires companies to recognize costs associated with exit or disposal activities when they are incurred rather than at the time that a commitment to an exit or disposal plan is made. Examples of costs covered by the statement include lease-termination expenses and certain employee-severance costs that are associated with a restructuring, discontinuing an operation, a plant closing, or other exit or disposal activities. SFAS No. 146 is to be applied prospectively to exit or disposal activities initiated after December 31, 2002.

In November, 2002, the FASB issued Interpretation (FIN) No. 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Guarantees of Indebtedness of Others." FIN No. 45 requires that certain guarantees be recorded at fair value and requires guarantors to make significant new disclosures, even if the likelihood of making payments under the guarantees is remote. The initial recognition and measurement provisions of FIN No. 45 are to be applied on a prospective basis for guarantees issued or modified after December 31, 2002. The disclosure requirements are effective for financial statements issued after December 15, 2002.

In December 2002, the FASB issued SFAS No. 148, "Accounting for Stock-Based Compensation – Transition and Disclosure." SFAS No. 148 delineates alternative transition approaches for companies electing to change their method of accounting for stock-based compensation costs to the fair-value method prescribed in SFAS No. 123. While not requiring companies to use the fair-value method of accounting for stock-based compensation, SFAS No. 148 does require companies to provide greater disclosure, including tabular presentation of pro forma net income and earnings per share as if the fair value method had been used for all periods presented, regardless of whether companies use SFAS No. 123's fair-value method or APB Opinion No. 25's intrinsic-value method. SFAS No. 148's transition and disclosure requirements are effective for quarterly and annual periods ending after December 15, 2002.

In January 2003, the FASB issued FIN No. 46, "Consolidation of Variable Interest Entities." FIN No. 46 addresses accounting for variable interest entities (VIEs), defined as separate legal structures that either do not have equity investors with voting rights or have equity investors with voting rights that do not provide sufficient financial resources for the entities to support their activities. FIN No. 46 requires that (1) a VIE be consolidated by a company if that company is subject to a majority of the VIE's gains and losses and (2) disclosures be made regarding VIEs that a company is not required to consolidate but in which it has a significant variable interest. Consolidation requirements apply immediately to VIEs created after January 31, 2003, and in the first fiscal year

or interim period beginning after June 15, 2003, for existing VIEs. Certain of the disclosure requirements apply to financial statements issued after January 31, 2003, regardless of when the VIE was created. Upon Pactiv's July 1, 2003, adoption of FIN No. 46, the company is likely to consolidate the VIE associated with the properties covered by its synthetic-lease facility, resulting in an increase in long-term debt and property, plant, and equipment of $169 million and $152 million, respectively. Consolidation of the VIE also would require the company to recognize, as a cumulative effect of change in accounting principles, depreciation expense on the leased assets from lease inception to June 30, 2003, which would negatively impact net income by approximately $10 million, or $0.06 per share. On a going-forward basis, consolidation of the VIE would reduce net income by approximately $3 million, or $0.02 per share, annually. See Note 17 for additional information on the company's synthetic-lease agreement.

Estimates

Financial-statement presentation requires management to make estimates and assumptions that affect reported amounts for assets, liabilities, sales, and expenses. Actual results may differ from such estimates.

Reclassifications

Certain prior-year amounts have been reclassified to conform with current-year presentation.

> NOTE 3 Restructuring and Other and Spin-off Transaction

Restructuring and Other

In the fourth quarter of 1999, the company recorded a $154 million restructuring charge, $91 million after tax, or $0.54 per share, related to the decision to exit noncore businesses and to reduce overhead costs. The restructuring covered (1) the sale of the company's forest-products and aluminum-foil container businesses ($68 million), for which cash proceeds of $20 million were received in the fourth quarter of 1999; (2) the sale of certain assets of the company's administrative service and corporate aircraft operations ($10 million); (3) the impairment of long-lived assets of the company's packaging-polyethylene business ($68 million); and (4) severance costs associated with the elimination of 161 positions, primarily in the company's international operations ($8 million). The impairment charge for the assets of the packaging-polyethylene business was deemed necessary following completion of an evaluation of strategic alternatives for the business and represented the difference between the carrying value of the assets and the forecasted future cash flows of the business, computed on a discounted basis. In the fourth quarter of 2000, $1 million of this charge was reversed, as one planned product-line consolidation was not undertaken and, as a result, 14 positions were not eliminated. With this exception, all restructuring actions were completed in 2000.

In the fourth quarter of 2000, the company recorded a restructuring charge of $71 million, $47 million after tax, or $0.29 per share. Of this amount, $45 million was for the impairment of assets held for sale, including those related to the packaging-polyethylene business and the company's interest in Sentinel Polyolefins LLC (Sentinel), a protective-packaging joint venture. In January 2001, the company received cash proceeds of $72 million from the disposition of these assets. The remaining $26 million was related to the realignment of operations and the exiting of low-margin businesses in the company's Protective and Flexible Packaging segment. Specifically, this charge was for (1) plant closures in North America and Europe, including the elimination of 202 positions ($6 million); (2) other workforce reductions (187 positions), mainly in Europe ($6 million); (3) impairment of European long-lived assets held for sale ($10 million); and (4) asset write-offs related to the elimination of certain low-margin product lines ($4 million). The impairment charge for European assets was recorded following completion of an evaluation of strategic alternatives for the related businesses and represented the difference between the carrying value of the assets and their fair value based on market estimates. Restructuring-plan actions have been completed. Actual cash outlays for severance and other costs were $3 million less than originally estimated, as 78 fewer positions were eliminated, while charges for asset write-offs were $3 million more than initially estimated. Additionally, the company recognized a benefit of $6 million, $4 million after tax, or $0.02 per share, in the fourth quarter of 2001, largely to reflect a lower loss than was originally recorded on the sale of the company's packaging-polyethylene business.

In the fourth quarter of 2001, the company recorded a restructuring charge of $18 million, $10 million after tax, or $0.06 per share. Of this amount, $5 million was related to higher-than-anticipated expenses associated with the exit of small, noncore European businesses announced in the fourth quarter of 2000. The remaining $13 million reflected adoption of a restructuring plan to consolidate operations and reduce costs in both the Consumer and Foodservice/Food Packaging ($5 million) and Protective and Flexible Packaging ($8 million) segments. Specifically, this charge was for (1) plant closures and consolidations in North America and Europe, including the elimination of 283 positions ($10 million); (2) other workforce reductions (99 positions—$2 million); and (3) asset writedowns related to the exit of a North American product line ($1 million).

In the second quarter of 2002, the company recognized a benefit of $4 million, $2 million after tax, or $0.02 per share, related to a previously recorded restructuring charge, primarily as a result of incurring a lower-than-anticipated loss on the sale of a noncore European business.

Amounts related to the restructuring activities are shown in the following table.

(In millions)	Severance	Asset impairment	Other	Total
Balance at December 31, 1999	8	–	1	9
2000 restructuring charge	10	56	5	71
Cash payments	(6)	–	–	(6)
Charged to asset accounts	–	(56)	–	(56)
Reversal of prior charge	–	–	(1)	(1)
Balance at December 31, 2000	12	–	5	17
2001 restructuring charge	6	11	1	18
Cash payments	(7)	–	(1)	(8)
Charged to asset accounts	–	(11)	–	(11)
Reversal of prior charge	(3)	(3)	–	(6)
Changes in estimates	(2)	3	(1)	–
Balance at December 31, 2001	$ 6	$ –	$ 4	$ 10
Cash payments	**(6)**	–	**(2)**	**(8)**
Balance at December 31, 2002	**$ –**	**$ –**	**$ 2**	**$ 2**

Spin-off Transaction Costs

In the fourth quarter of 1999, the company recorded transaction costs related to its spin-off from Tenneco Inc. (Tenneco) in 1999 that reduced income before interest expense, income taxes, and minority interest; net income; and earnings per share by $136 million, $96 million, and $0.57, respectively. These costs pertained to special curtailment and termination benefits for former Tenneco employees ($72 million), professional services ($49 million), and separation from Tenneco operations ($15 million). In the fourth quarters of 2000 and 2001, the company reversed $20 million, $12 million after tax, or $0.08 per share, and $12 million, $7 million after tax, or $0.04 per share, respectively, of the previously recorded spin-off transaction costs to reflect lower-than-anticipated expenses. Actions related to the spin-off transaction have been completed.

> NOTE 4 Acquisitions and Dispositions

In December 1999, the company entered into an agreement to sell its aluminum-foil reroll facility in Clayton, New Jersey, and its aluminum packer-processor facility in Shelbyville, Kentucky, for $44 million. The company recorded a related gain of $6 million, $4 million after tax, or $0.02 per share, during 2000, and used the proceeds from the transaction to repay debt.

The company recorded a fourth-quarter 2000 charge of $45 million, $29 million after tax, or $0.18 per share, to recognize the impairment of assets held for sale, including those related to the packaging-polyethylene business and the company's interest in Sentinel. In January 2001, the company received cash proceeds of $72 million from the disposition of these assets. In the third quarter of 2001, the company refunded $7 million to the purchaser of the packaging-polyethylene business to reflect the final determination of certain asset and liability amounts. Also, as part of the company's 2000 restructuring plan, certain small, noncore European businesses were disposed of in 2001 and 2002, for which cash proceeds totaling $6 million and $5 million were received in December 2001 and May 2002, respectively. See Note 3 for additional information.

On January 4, 2002, the company purchased MSP Schmeiser GmbH, a German medical-products company, for $3 million. On February 13, 2002, the company acquired an egg-packaging production line from Amerpack S.A. de C.V., a Mexican company, for $10 million.

In January 2002, the company purchased the assets of 2 small Italian protective-packaging companies, recording these transactions as capital expenditures. The outstanding shares of a third small Italian protective-packaging company, Forniture Industriali, were acquired in June 2002, for $1 million.

On June 18, 2002, the company purchased Winkler Forming Inc. (Winkler), a leading thermoformer of amorphous polyethylene terephthalate (APET) products for food packaging, for $78 million. During the third quarter of 2002, the company received $3 million from the seller in interim settlement of working capital amounts. At December 31, 2002, the allocation of the purchase price to the net assets of Winkler and the related recognition of $55 million of goodwill were based on preliminary estimates of the fair-market value of the assets and liabilities acquired, and, therefore, are subject to revision based on final appraisals.

On October 21, 2002, Pactiv completed the purchase of 70% of the stock of Mexico-based Central de Bolsas, S.A. de C.V. (Jaguar), a leading thermoformer of high-impact polystyrene (HIPS) for cold cups and plates and polystyrene foam for foodservice/food packaging. For this 70% interest, Pactiv paid $31 million to the shareholders of Jaguar and made a $20 million equity investment in Jaguar. At December 31, 2002, the allocation of the purchase price to the net assets of Jaguar and the related recognition of $7 million of goodwill were based on preliminary estimates of the fair market value of the assets and liabilities acquired, and, therefore, are subject to revision based on final appraisals.

On November 13, 2002, Pactiv purchased the shares of Prvni Obalova SPOL S.R.O, a distributor and converter of protective-packaging products in the Czech Republic, for $4 million.

The following unaudited pro forma information summarizes the results of operations for the 12 months ended December 31, 2002, and 2001, as if fiscal 2002 acquisitions had been completed as of the beginning of the respective periods. The pro forma data presented reflect actual operating results of the acquired businesses, with adjustments recorded for depreciation, interest expense, and income taxes. Excluded from the pro forma data is the potential impact of cost reductions or operating synergies. These pro forma amounts are not necessarily indicative of the results that would have actually been achieved had the acquisitions occurred at the beginning of the periods presented, or that may be achieved in the future.

	Pro forma	
Years ended December 31 (In millions, except earnings per share)	**2002**	**2001**
Sales	**$2,971**	$2,963
Income from continuing operations	**220**	168
Net income	**148**	196
Earnings per share		
Continuing operations	**1.37**	1.05
Net	**0.92**	1.22

> NOTE 5 **Discontinued Operations**

In April 1999, the company contributed the containerboard assets of its paperboard packaging operations to a newly formed joint venture, Packaging Corporation of America (PCA). For the contribution, Pactiv, along with other consideration, received a 45% equity interest in PCA.

In February 2000, the company sold 85% of its equity interest in PCA and used the net proceeds of $398 million primarily to repay debt. The company recorded a related gain of $224 million, $134 million after tax, or $0.80 per share. In the first half of 2001, the company sold its remaining interest in PCA for $87 million, which was used primarily to repay debt, and recorded an associated gain of $57 million, $28 million after tax, or $0.17 per share.

The company provides office space and certain administrative services to PCA under a transition-service agreement.

Net assets as of December 31, 2001, and 2000, and results of operations for the years then ended for the company's discontinued paperboard packaging operations were as follows:

Years ended December 31 (In millions)	**2001**	**2000**
Net assets	$ –	$ 72
Gain on sale of PCA stock	57	224
Income before interest and income taxes	57	224
Income tax expense	29	90
Income from discontinued operations	$ 28	$ 134

Pactiv has retained responsibility for certain contingent liabilities of its former paperboard-packaging businesses and has recorded related reserves where, in the judgment of management, it is probable that a quantifiable liability exists. Management believes that these liabilities will not have a material effect on the results of operations or financial position of the company.

In connection with the formation of the PCA joint venture, Pactiv entered into a 5-year agreement to purchase corrugated products from PCA on an arm's length basis.

> NOTE 6 **Long-Term Debt, Short-Term Debt, and Financing Arrangements**

Long-Term Debt

December 31 (In millions)	**2002**	**2001**
Pactiv Corporation		
Borrowings under 5-year, $750 million revolving-credit agreement, effective interest rate based on LIBOR plus 0.7%	**$ 36**	$ 36
Notes due 2005, effective interest rate of 7.2%, net of $3 million unamortized discount	**296**	295
Notes due 2007, effective interest rate of 8.0%	**98**	98
Debentures due 2017, effective interest rate of 8.1%	**300**	300
Debentures due 2025, effective interest rate of 8.0%, net of $1 million unamortized discount	**275**	275
Debentures due 2027, effective interest rate of 8.4%, net of $4 million unamortized discount	**196**	196
Subsidiaries		
Notes due 2003 through 2016, average effective interest rate of 4.0% in 2002 and 9.0% in 2001	**31**	14
Less current maturities	**(8)**	(3)
Total long-term debt	**$1,224**	$1,211

Aggregate maturities of debt outstanding at December 31, 2002, are $8 million, $43 million, $307 million, $7 million, $99 million, and $776 million for 2003, 2004, 2005, 2006, 2007, and thereafter, respectively.

At December 31, 2002, the total amount of floating-rate, long-term debt was $36 million. As of December 31, 2002, the company was in full compliance with financial and other covenants in its various credit agreements.

Short-Term Debt

December 31 (In millions)	**2002**	**2001**
Current maturities of long-term debt	**$ 8**	$ 3
Other	**5**	4
Total short-term debt	**$ 13**	$ 7

The company uses lines of credit and overnight borrowings to finance certain of its short-term capital requirements. Information regarding short-term debt is shown below.

(Dollars in millions)	2002 (a)	2001 (a)
Borrowings at end of year	$ 5	$ 4
Weighted-average interest rate on borrowings at end of year	10.0%	10.8%
Maximum month-end borrowings during year	7	27
Average month-end borrowings during year	3	11
Weighted-average interest rate on average month-end borrowings during year	8.1%	8.1%

(a) Includes borrowings under committed credit facilities and uncommitted lines of credit.

Financing Arrangements

	Committed credit facilities (a)			
(Dollars in millions)	Term	Commitments	Utilized	Available
Credit agreements				
5-year revolving-credit agreement	2004	$ 750	$36	$ 714

(a) Agreements call for the payment of utilization fees on borrowings and facility fees on commitments.

In conjunction with the 1999 realignment of Tenneco debt, the company paid bank-facility fees of $10 million and entered into an interest-rate swap to hedge its exposure to interest-rate movement. The company settled this swap in November 1999 at a loss of $43 million. Both the loss on the swap and the bank-facility fees are being recognized as additional interest expense over the average life of the underlying debt.

> NOTE 7 Financial Instruments

Asset and Liability Instruments

At December 31, 2002, and 2001, the fair value of cash and temporary cash investments, short- and long-term receivables, accounts payable, and short-term debt were considered to be the same as, or not materially different from, amounts recorded for these assets and liabilities. The fair value of long-term debt at December 31, 2002, was approximately $1,427 million, compared with its recorded amount of $1,224 million. At December 31, 2001, the fair value of long-term debt was not materially different from its recorded amount. The fair value of long-term debt was based on quoted market prices for the company's debt instruments.

Instruments with Off-Balance-Sheet Risk

From time to time, Pactiv enters into foreign-currency forward contracts with terms of less than 1 year to mitigate its exposure to exchange-rate changes related to third-party trade receivables and accounts payable. The following table summarizes foreign-currency contracts entered into by the company at December 31, 2002.

	Notional amount	
(In millions)	Purchase	Sell
Foreign-currency contracts		
Euro	$ 50	$ 3
British pounds	3	49
	$ 53	$ 52

Based on exchange rates at December 31, 2002, the cost of replacing these contracts in the event of nonperformance by counter parties would not be material.

In the first quarter of 2001, the company entered into interest-rate swap agreements to convert floating-rate debt on its synthetic-lease obligations to fixed-rate debt. This action was taken to reduce the company's exposure to interest-rate risk. As of December 31, 2001, $5 million of deferred net losses on derivative instruments was recorded in other comprehensive income.

During the first quarter of 2002, the company exited these swap agreements, and related accumulated deferred net losses of $2 million at December 31, 2002, will be expensed over the remaining life of the underlying obligations.

Lines of Credit and Guarantees

The company, from time to time, utilizes various short-term lines of credit to finance operations. Total committed lines of credit were $36 million and $31 million at December 31, 2002, and December 31, 2001, respectively. Certain lines of credit are backed by payment and performance guarantees. Borrowings under lines of credit were not material at December 31, 2002, or December 31, 2001.

> NOTE 8 Inventories

December 31 (In millions)	2002	2001
Finished goods	$ 244	$ 209
Work in process	47	43
Raw materials	42	50
Other materials and supplies	35	30
	$ 368	$ 332

> NOTE 9 Goodwill and Intangible Assets

Effective January 1, 2002, the company adopted SFAS No. 142. In this connection, the company completed a review of its businesses and tested recorded goodwill amounts for possible impairment. Goodwill was found to be impaired for certain Protective and Flexible Packaging businesses that were acquired prior to the company's spin-off from Tenneco. These businesses have recently faced increased competition and experienced lower operating margins. As a result, the company recorded a goodwill-impairment charge of $83 million, $72 million after tax, or $0.45 per share, in the first quarter of 2002.

In accordance with requirements of SFAS No. 142, the company discontinued the amortization of goodwill effective January 1, 2002. Shown below is a comparison of income from continuing operations, net income, and earnings per share (EPS) for 2002 with corresponding amounts recorded in 2001and 2000 adjusted to exclude the amortization of goodwill.

(In millions, except per-share data)	2002	2001	2000
Income from continuing operations	$ 220	$ 165	$ 113
Goodwill amortization, net of tax	–	14	14
Adjusted income from continuing operations	220	179	127
Income from discontinued operations, net of tax	–	28	134
Cumulative effect of change in accounting principles, net of tax	(72)	–	–
Pro forma net income	$ 148	$ 207	$ 261
Basic EPS			
Continuing operations	$ 1.38	$ 1.04	$ 0.70
Goodwill amortization	–	0.09	0.08
Adjusted continuing operations	1.38	1.13	0.78
Discontinued operations	–	0.17	0.83
Cumulative effect of change in accounting principles	(0.45)	–	–
Pro forma EPS	$ 0.93	$ 1.30	$ 1.61
Diluted EPS			
Continuing operations	$ 1.37	$ 1.03	0.70
Goodwill amortization	–	0.09	0.08
Adjusted continuing operations	1.37	1.12	0.78
Discontinued operations	–	0.17	0.83
Cumulative effect of change in accounting principles	(0.45)	–	–
Pro forma EPS	$ 0.92	$ 1.29	$ 1.61

Changes in the carrying value of goodwill during 2002 by operating segment are shown in the following table.

(In millions)	Consumer and Foodservice/ Food Packaging	Protective and Flexible Packaging	Total
Balance, December 31, 2001	$ 376	$ 239	$ 615
Goodwill impairment	–	(83)	(83)
Goodwill addition	62	9	71
Translation adjustment	–	9	9
Balance, December 31, 2002	$ 438	$ 174	$ 612

Intangible assets at December 31, 2002, are shown in the following table.

(Dollars in millions)	Weighted average life (years)	Carrying amount	Accumulated amortization	Total
Intangible assets subject to amortization:				
Patents	21.6	$ 186	$ 60	$ 126
Other	13.4	58	19	39
		244	79	165
Intangible assets not subject to amortization (primarily trademarks)		129	–	129
Total intangible assets		$ 373	$ 79	$ 294

Amortization expense for intangible assets was $18 million for the year ended December 31, 2002. Amortization expense is estimated to total $12 million, $12 million, $12 million, $11 million, and $11 million for 2003, 2004, 2005, 2006, and 2007, respectively.

NOTE 10 Property, Plant, and Equipment, Net

December 31 (In millions)	2002	2001
Original cost		
Land, buildings, and improvements	$ 573	$ 475
Machinery and equipment	1,673	1,311
Other, including construction in progress	225	159
	2,471	1,945
Less accumulated depreciation and amortization	(1,105)	(672)
	$1,366	$1,273

> NOTE 11 **Income Taxes**

The domestic and foreign components of income (loss) from continuing operations before income taxes were as follows:

(In millions)	2002	2001	2000
U.S. income before income taxes	$ 325	$ 276	$ 215
Foreign income (loss) before income taxes	42	8	(8)
Total income before income taxes	$ 367	$ 284	$ 207

Following is a comparative analysis of the components of income tax expense applicable to continuing operations.

(In millions)	2002	2001	2000
Current			
Federal	$ 25	$ 2	$ 10
State and local	10	5	2
Foreign	9	(1)	7
	44	6	19
Deferred			
Federal	88	98	69
State and local	6	9	10
Foreign	8	5	(7)
	102	112	72
Total income tax expense	$ 146	$ 118	$ 91

A reconciliation of the difference between the U.S. statutory federal income tax rate and the company's effective income tax rate is shown in the following table.

	2002	2001	2000
U.S. federal income tax rate	35.0%	35.0%	35.0%
Increase in income tax rate resulting from:			
Foreign income taxed at various rates	0.5	0.4	0.5
State and local taxes on income, net of U.S. federal income tax benefit	2.9	3.1	3.4
Amortization of nondeductible goodwill	–	1.1	3.4
Other	1.6	1.9	1.7
Effective income tax rate	40.0%	41.5%	44.0%

Summarized below are the components of the company's net deferred tax liability.

December 31 (In millions)	2002	2001
Deferred tax assets		
Tax-loss carryforwards		
U.S.	$ –	$ 2
State and local	1	1
Foreign	13	17
Alternative minimum tax-credit carryforward	–	26
Pensions	130	–
Postretirement benefits	28	51
Restructuring reserves	1	17
Other items	57	55
Valuation allowance	(12)	(13)
Total deferred tax assets	218	156
Deferred tax liabilities		
Property and equipment	250	229
Pensions	–	390
Other items	85	74
Total deferred tax liabilities	335	693
Net deferred tax liabilities	$ 117	$ 537

The company had $43 million of foreign tax-loss carryforwards at December 31, 2002, of which $27 million will expire at various dates from 2003 to 2012, with the remainder having unlimited lives. At December 31, 2002, the company had $15 million of state tax-loss carryforwards, which will expire at various dates from 2003 to 2012.

The valuation allowance for deferred tax assets ($12 million at December 31, 2002) was recorded to recognize the potential inability to utilize certain foreign tax-loss carryforwards.

Common Stock

The company has 350 million shares of common stock ($0.01 par value) authorized, of which 158,681,918 shares were issued and outstanding as of December 31, 2002.

Reserves

Reserved shares (In thousands)

Thrift plans	2,468
2002 incentive-compensation plan	26,911
Employee stock-purchase plan	2,779
	32,158

Stock Plans

2002 Incentive-Compensation Plan - In November 1999, the company initiated a stock-ownership plan that permits the granting of a variety of awards, including common stock, restricted stock, performance shares, stock appreciation rights, and stock options to directors, officers, and employees. In May 2002, the 1999 plan was succeeded by the 2002 incentive compensation plan and all share balances were transferred to the new plan, which will remain in effect until amended or terminated. Under the 2002 plan, up to 27 million shares of common stock can be issued (including shares issued under the prior plan), of which 15 million had been issued or granted as of December 31, 2002.

Restricted-stock, performance-share, and stock-option awards generally require that, among other things, grantees remain with the company for certain periods of time. Performance shares granted under the plan vest upon the attainment of specified performance goals in the 3 years following the date of grant.

Details of performance- and restricted-stock balances are shown below.

	Performance shares	Restricted shares
Outstanding, January 1, 2001	144,000	30,238
Granted	394,557	–
Canceled	(10,665)	–
Outstanding, December 31, 2001	527,892	30,238
Granted	100,433	2,500
Canceled	(11,733)	–
Vested	–	(32,738)
Outstanding, December 31, 2002	616,592	–

Summarized below are stock options issued by Pactiv.

	Shares under option	Weighted-average exercise price
Outstanding, January 1, 2001	12,392,842	$24.34
Granted	2,509,382	16.23
Exercised	(33,283)	12.59
Canceled	(1,440,436)	29.64
Outstanding, December 31, 2001	13,428,505	22.29
Exercisable, December 31, 2001	5,607,768	32.00
Outstanding, January 1, 2002	13,428,505	22.29
Granted	2,288,917	17.65
Exercised	(420,064)	12.79
Canceled	(1,109,985)	30.41
Outstanding, December 31, 2002	14,187,373	21.19
Exercisable, December 31, 2002	9,324,775	23.23

Stock options expire 10 to 20 years following date of grant and vest over periods ranging from 1 to 3 years.

The weighted-average fair value of options granted by the company in 2002 ($6.17), 2001 ($6.15), and 2000 ($4.57) was determined using the Black-Scholes option-pricing model with the following assumptions:

	2002	2001	2000
Actuarial assumptions			
Risk-free interest rate	3.0%	4.3%	5.9%
Life	4.4 years	4.4 years	5.0 years
Volatility	38.7%	41.1%	36.6%

Summarized below is information about stock options outstanding at December 31, 2002.

	Outstanding options			Exercisable options	
	Number	Weighted-average remaining contractual life	Weighted-average exercise price	Number	Weighted-average exercise price
Range of exercise price					
$ 7 to $12	2,051,452	7.8 years	$11.65	1,322,728	$11.64
$13 to $21	8,069,729	8.2	15.47	4,270,073	14.00
$22 to $29	15,000	9.4	22.79	–	22.79
$30 to $37	1,824,885	11.2	34.22	1,505,667	34.22
$38 to $45	2,226,307	8.0	40.00	2,226,307	40.00
	14,187,373			9,324,775	

See Note 2 for additional information regarding accounting for stock-based employee compensation.

Employee Stock-Purchase Plan - The company has a stock-purchase plan that allows U.S. and Canadian employees to purchase Pactiv common stock at a 15% discount, subject to an annual limitation of $21,240. In 2002, 2001, and 2000, employees purchased 401,469 shares, 448,910 shares, and 463,412 shares, respectively, of Pactiv stock at a weighted-average price of $14.68, $10.46, and $7.25, respectively.

Grantor Trust - In November 1999, the company established a grantor trust and reserved 3,200,000 shares of Pactiv common stock for the trust. These shares were issued to the trust in January 2000. This so-called "rabbi trust" is designed to assure the payment of deferred-compensation and supplemental-pension benefits. These shares are not considered to be outstanding for purposes of financial reporting.

Qualified Offer Rights Plan

In November 1999, Pactiv adopted a qualified offer rights plan (QORP) to deter coercive takeover tactics and to prevent a potential acquirer from gaining control of the company in a transaction that would not be in the best interests of shareholders. Under the plan, if a person becomes the beneficial owner of 20% or more of the company's outstanding common stock, other than pursuant to a qualified offer, each right will entitle its holder to purchase common stock having a market value of twice the right's exercise price, but rights held by the 20%-or-more holder would not be exercisable.

Rights are not exercisable in connection with a qualified offer, which is defined as an all-cash tender offer for all outstanding shares of common stock that is fully financed, remains open for a period of at least 60 business days, results in the offeror owning at least 85% of the common stock after consummation of the offer, assures a prompt second-step acquisition of shares not purchased in the initial offer at the same price as the initial offer, and meets certain other requirements.

In connection with the adoption of the QORP, the board of directors also adopted an evaluation mechanism that calls for an independent board committee to review, on an ongoing basis, the QORP and developments in rights plans in general and, if it deems appropriate, to recommend modification or termination of the plan. The independent committee is required to report to the board at least every 3 years as to whether the QORP continues to be in the best interest of shareholders.

Earnings Per Share

Earnings from continuing operations per share of common stock outstanding were computed as follows:

(In millions, except share and per-share data)	2002	2001	2000
Basic earnings per share			
Income from continuing operations	**$ 220**	$ 165	$ 113
Average number of shares of common stock outstanding	**158,618,274**	158,833,296	161,722,021
Basic earnings from continuing operations per share	**$ 1.38**	$ 1.04	$ 0.70
Diluted earnings per share			
Income from continuing operations	**$ 220**	$ 165	$ 113
Average number of shares of common stock outstanding	**158,618,274**	158,833,296	161,722,021
Effect of dilutive securities			
Restricted stock	**–**	18,097	–
Stock options	**1,579,885**	498,634	1,406
Performance shares	**414,916**	177,143	55,313
Average number of shares of common stock outstanding including dilutive securities	**160,613,075**	159,527,170	161,778,740
Diluted earnings from continuing operations per share	**$ 1.37**	$ 1.03	$ 0.70

In accordance with a stock-repurchase plan announced in February 2000, the company acquired 11,742,951 shares of its common stock in 2000 at an average price of $8.50 per share for a total outlay of $100 million. In 2002, the company acquired 2,119,009 shares of its common stock at an average price of $19.20 per share, for a total outlay of $40 million.

> NOTE 13 Preferred Stock

Pactiv has 50 million shares of preferred stock ($0.01 par value) authorized, none of which were issued at December 31, 2002. The company has reserved 750,000 shares of preferred stock in connection with the QORP.

> NOTE 14 Minority Interest

In December 2001, the company purchased for $15 million the outstanding shares of Astro-Valcour, Inc., whose sole asset was the preferred stock of a Pactiv subsidiary that was issued to it in 1997 in connection with the company's acquisition of the packaging business of N.V. Koninklijke KNP BT. This amount had previously been recorded as minority interest in the company's statement of financial position. In October 2002, the company acquired a 70% interest in Jaguar and recorded a related minority interest of $13 million.

> NOTE 15 Pension Plans and Other Postretirement Benefits

The company has pension plans that cover substantially all of its employees. Benefits are based on years of service and, for most salaried employees, final-average compensation. The company's funding policy is to contribute to the plans amounts necessary to satisfy requirements of applicable laws and regulations. Plan assets consist principally of equity and fixed-income securities and included 4,113,548 shares of Pactiv stock with a fair-market value of $90 million at December 31, 2002. These shares were contributed by Tenneco prior to the spin-off. Effective with the spin-off, Pactiv became the sponsor of Tenneco's retirement plans, receiving related assets and assuming the obligation to provide pension benefits to participating employees of Tenneco Automotive Inc. and certain former subsidiaries and affiliates of Tenneco. For Tenneco Automotive Inc. employees, benefits accrued under these plans were frozen as of November 30, 1999.

The company has postretirement health-care and life-insurance plans that cover certain of its salaried and hourly employees. For salaried employees, the plans cover individuals who retire on or after reaching age 55 with at least 10 years of service after reaching age 45. For hourly employees, postretirement-benefit plans cover individuals who retire in accordance with the various provisions of such plans. Benefits may be subject to deductibles, copayments, and other limitations. The company reserves the right to change postretirement plans, which are not funded.

Financial data pertaining to the company's pension and postretirement benefit plans appear below.

(In millions)	Pension plans 2002	Pension plans 2001	Postretirement plans 2002	Postretirement plans 2001
Changes in projected benefit obligations				
Benefit obligations at September 30 of the previous year	**$ 3,390**	$ 3,195	**$ 96**	$ 77
Currency-rate conversion	**7**	(2)	**–**	–
Service cost of benefits earned	**35**	30	**1**	1
Interest cost on benefit obligations	**237**	231	**7**	10
Plan amendments	**–**	6	**(10)**	11
Actuarial losses	**216**	166	**18**	8
Benefits paid	**(239)**	(236)	**(12)**	(12)
Participant contributions	**–**	–	**2**	1
Divestitures	**(2)**	–	**–**	–
Benefit obligations at September 30	**$ 3,644**	$ 3,390	**$ 102**	$ 96
Changes in fair value of plan assets				
Fair value at September 30 of the previous year	**$ 3,561**	$ 4,508	**$ –**	$ –
Currency rate conversion	**5**	(2)	**–**	–
Actual return on plan assets	**(269)**	(709)	**–**	–
Employer contributions	**(1)**	(1)	**10**	11
Participant contributions	**1**	1	**2**	1
Benefits paid	**(239)**	(236)	**(12)**	(12)
Divestitures	**(1)**	–	**–**	–
Fair value at September 30	**$ 3,057**	$ 3,561	**$ –**	$ –
Development of amounts recognized in the statement of financial position				
Funded status at September 30	**$ (587)**	$ 171	**$ (102)**	$ (96)
Contributions during the fourth quarter	**1**	(8)	**3**	3
Unrecognized cost				
Actuarial losses	**1,722**	851	**45**	30
Prior-service costs	**20**	28	**(2)**	9
Transition asset	**–**	(1)	**–**	–
Net amount recognized at December 31	**$1,156**	$ 1,041	**$ (56)**	$ (54)
Amounts recognized in the statement of financial position				
Prepaid benefit cost	**$ 170**	$ 1,070	**$ –**	$ –
Accrued benefit cost	**(542)**	(36)	**(56)**	(54)
Intangible assets	**18**	1	**–**	–
Accumulated other comprehensive income	**1,510**	6	**–**	–
Net amount recognized at December 31	**$ 1,156**	$ 1,041	**$ (56)**	$ (54)

The impact of pension plans on income from continuing operations was as follows:

(In millions)	2002	2001	2000
Service cost of benefits earned	**$ (35)**	$ (30)	$ (30)
Interest cost on benefit obligations	**(237)**	(231)	(224)
Expected return on plan assets	**385**	373	349
Prior-service cost	**(5)**	(5)	(6)
SFAS No. 87 transition gain	**1**	6	19
Total pension-plan income	**$ 109**	$ 113	$ 108

Actuarial assumptions used for the pension plans are shown below.

September 30	2002	2001	2000
Actuarial assumptions			
Discount rate	**6.75%**	7.25%	7.5%
Compensation increases	**4.9**	4.9	4.9
Return on assets	**9.0**	9.5	9.5

For pension plans with accumulated benefit obligations in excess of plan assets, the projected benefit obligations, accumulated benefit obligations, and fair value of plan assets were $3,326 million, $3,252 million, and $2,711 million, respectively, at September 30, 2002, and $84 million, $74 million, and $39 million, respectively, at September 30, 2001.

The impact of postretirement-benefit plans on continuing operations was as follows:

(In millions)	2002	2001	2000
Service cost of benefits earned	**$ 1**	$ 1	$ 1
Interest cost on benefit obligations	**6**	6	5
Prior-service cost	**2**	–	–
Loss	**2**	5	1
Total postretirement-benefit plan costs	**$ 11**	$ 12	$ 7

Actuarial assumptions used to determine postretirement-benefit obligations follow:

	2002	2001	2000
Actuarial assumptions			
Health-care cost inflation trend (a)	**12.0%**	10.0%	5.0%
Discount rate	**6.75**	7.25	7.5

(a) Assumed to decline to 5% over 5 years.

Increasing the assumed health-care cost inflation rate 1% each year would increase 2002, 2001, and 2000 postretirement-benefit obligations by approximately $2 million each year; however, the aggregate of service and interest costs would not change for 2002, 2001, or 2000.

Decreasing the assumed health-care cost inflation rate 1% each year would decrease 2002, 2001, and 2000 postretirement-benefit obligations by approximately $2 million each year, but would not change the aggregate of service and interest costs for 2002, 2001, or 2000.

In accordance with current Employee Retirement Income Security Act regulations, the company funded $9 million of its postretirement-benefit obligations with excess pension-plan assets in 2001.

> NOTE 16 Segment and Geographic-Area Information

The company has three operating segments: Consumer and Foodservice/Food Packaging, which relates to the manufacture and sale of disposable plastic, molded-fibre, pressed-paperboard, and aluminum packaging products for the consumer, foodservice, and food-packaging markets; Protective and Flexible Packaging, which relates to the manufacture and sale of plastic, paperboard, and molded-fibre products for protective-packaging markets such as electronics, automotive, furniture, and e-commerce, and for flexible-packaging applications in food, medical, pharmaceutical, chemical, and hygienic markets; and Other, which relates to corporate and administrative service operations and retiree-benefit income and expense.

The accounting policies of the segments are the same as those described in Note 2. Products are transferred between segments and among geographic areas at, as nearly as possible, market value. In 2002, Wal-Mart Stores, Inc. accounted for 10.0% of the company's sales. In general, the company's backlog of orders is not material.

The following table sets forth certain segment information.

(In millions)	Segment: Consumer and Foodservice/ Food Packaging	Segment: Protective and Flexible Packaging	Segment: Other	Reclassifications and eliminations	Total
At December 31, 2002, and for the year then ended					
Sales to external customers	**$ 2,062**	**$ 818**	**$ –**	**$ –**	**$ 2,880**
Depreciation and amortization	**122**	**30**	**6**	**–**	**158**
Income before interest, income taxes, and minority interest	**346(a)**	**62(b)**	**55(c)**	**–**	**463**
Cumulative effect of change in accounting principles	**–**	**(72)**	**–**	**–**	**(72)**
Total assets	**2,057**	**713**	**642(d)**	**–**	**3,412**
Investment in affiliated companies	**1**	**3**	**–**	**–**	**4**
Capital expenditures	**84**	**39**	**3**	**–**	**126**
Noncash items other than depreciation and amortization	**–**	**(4)**	**(109)(e)**	**–**	**(113)**
At December 31, 2001, and for the year then ended					
Sales to external customers	$ 1,997	$ 815	$ –	$ –	$ 2,812
Depreciation and amortization	129	38	10	–	177
Income before interest, income taxes, and minority interest	288(a)	29(b)	74(c)	–	391
Income from discontinued operations	–	–	28	–	28
Total assets	2,005	729	1,451(d)	(125)	4,060
Investment in affiliated companies	1	1	–	–	2
Capital expenditures	112	27	6	–	145
Noncash items other than depreciation and amortization	(7)	14	(106)(e)	–	(99)
At December 31, 2000, and for the year then ended					
Sales to external customers	$ 2,201	$ 851	$ –	$ –	$ 3,052
Depreciation and amortization	131	43	11	–	185
Income before interest, income taxes, and minority interest	254(a)	5(b)	82(c)	–	341
Income from discontinued operations	–	–	134	–	134
Total assets	1,989	827	1,496(d)	(89)	4,223
Net assets of discontinued operations	–	–	72	–	72
Investment in affiliated companies	1	2	–	–	3
Capital expenditures	106	27	2	–	135
Noncash items other than depreciation and amortization	26	29	(113)(e)	–	(58)

(a) Includes restructuring and other charges (credits) of $(1) million and $31 million in 2001 and 2000, respectively.

(b) Includes restructuring and other charges (credits) of $(4) million, $13 million, and $39 million in 2002, 2001, and 2000, respectively.

(c) Includes pension-plan income; unallocated corporate expenses; and spin-off transaction cost reversals of $12 million and $20 million in 2001 and 2000, respectively.

(d) Includes assets related to pension plans and administrative service operations.

(e) Includes pension-plan income.

The following table sets forth certain geographic-area information.

(In millions)	Geographic area United States	Foreign(a)	Reclassifications and eliminations	Total
At December 31, 2002, and for the year then ended				
Sales to external customers (b)	**$ 2,286**	**$ 594**	**$ –**	**$ 2,880**
Long-lived assets (c)	**1,298**	**304**	**–**	**1,602**
Total assets	**2,756**	**656**	**–**	**3,412**
At December 31, 2001, and for the year then ended				
Sales to external customers (b)	$ 2,262	$ 550	$ –	$ 2,812
Long-lived assets (c)	2,203	186	–	2,389
Total assets	3,560	537	(37)	4,060
At December 31, 2000, and for the year then ended				
Sales to external customers (b)	$ 2,490	$ 562	$ –	$ 3,052
Long-lived assets (c)	2,189	217	–	2,406
Total assets	3,775	601	(35)	4,341

(a) Sales to external customers and long-lived assets for individual countries (primarily in Europe) were not material.
(b) Geographic assignment is based on location of selling business.
(c) Long-lived assets include all long-term assets other than net assets of discontinued operations, goodwill, intangibles, and deferred taxes.

> NOTE 17 Commitments and Contingencies

Capital Commitments

The company estimates that the completion of projects authorized at December 31, 2002, and for which commitments have been made will require expenditures of approximately $90 million in 2003.

Purchase Commitments

The company occasionally enters into short-term forward contracts with third parties to fix a portion of the cost of certain commodities used internally. Several of such contracts for aluminum remained open at December 31, 2002.

Lease Commitments

Pactiv has entered into a $169 million synthetic-lease agreement with a third-party lessor and various lenders to finance the cost of its headquarters building and certain of its warehouse facilities and to facilitate additional leasing arrangements for other operating facilities. This agreement, which will expire in November 2005, contains customary terms and conditions covering, among other things, residual-value guarantees, default provisions, and financial covenants, and requires that certain financial-ratio tests be satisfied. Upon expiration of the initial lease periods for the properties, the company may extend the leases on terms negotiated with the lessors or purchase the leased assets under specified conditions. Termination of the synthetic-lease agreement, either before or at expiration, would require the company to make a termination payment of $169 million, which, in essence, represents off-balance-sheet debt in that the company might be required to obtain alternative financing to fund such a payment.

Annual lease payments under the synthetic-lease agreement are expected to total approximately $4 million in 2003, 2004, and 2005.

Certain of the company's facilities, equipment, and other assets are leased under long-term arrangements. Minimum lease payments under noncancelable operating leases with lease terms in excess of 1 year are expected to total $33 million, $25 million, $17 million, $13 million, and $12 million for 2003, 2004, 2005, 2006, and 2007, respectively; and $27 million for subsequent years.

Commitments under capital leases are not significant. Total rental costs for continuing operations for 2002, 2001, and 2000 were $42 million, $40 million, and $43 million, respectively, which included minimum rentals under noncancelable operating leases of $36 million, $35 million, and $33 million for the respective periods.

Litigation

In May 1999, Tenneco, Pactiv (through Tenneco's former paperboard-packaging operations), and a number of containerboard manufacturers were named as defendants in a civil, class-action antitrust lawsuit pending in the U.S. district court for the Eastern District of Pennsylvania. The company also was named as a defendant in a related class-action antitrust lawsuit. The lawsuits allege that the defendants conspired to raise linerboard prices for corrugated containers and corrugated sheets from October 1, 1993, through November 30, 1995, in violation of Section 1 of the Sherman Act. The lawsuits seek treble damages of unspecified amounts, plus attorneys' fees. Pactiv's management believes that the allegations have no merit and is vigorously defending the claims.Tenneco sold its containerboard business in April 1999, prior to the spin-off of Pactiv in November 1999. In connection with the spin-off, Pactiv was assigned responsibility for defending the claims against Tenneco with respect to such lawsuit and for any liability resulting therefrom.

The company is party to other legal proceedings arising from its operations.

Management believes that the outcome of all of these legal matters, individually and in the aggregate, will not have a material adverse effect on the company's earnings or financial position.

Environmental Matters

The company is subject to a variety of environmental and pollution-control laws and regulations in all jurisdictions in which it operates. Pactiv provides related reserves where it is probable that liabilities exist and where reasonable estimates of the liabilities can be made. Estimated liabilities are subject to change as more information becomes available regarding the magnitude of possible clean-up costs and the cost and effectiveness of alternative clean-up technologies. However, management believes that any additional costs that may be incurred as more information becomes available will not have a material effect on the earnings or financial condition of the company.

> NOTE 18 Quarterly Financial Data (Unaudited)

(In millions)	Sales	Cost of sales	Income from continuing operations	Income from discontinued operations	Cumulative effect of change in accounting principles	Net income
2002						
First quarter	**$ 647**	**$ 438**	**$ 42**	**$ –**	**$ (72)**	**$ (30)**
Second quarter	**728**	**494**	**60**	**–**	**–**	**60**
Third quarter	**727**	**499**	**59**	**–**	**–**	**59**
Fourth quarter	**778**	**536**	**59**	**–**	**–**	**59**
	$ 2,880	**$ 1,967**	**$ 220**	**$ –**	**$ (72)**	**$ 148**
2001						
First quarter	$ 680	$ 489	$ 29	$ 4	$ –	$ 33
Second quarter	728	510	45	24	–	69
Third quarter	694	475	45	–	–	45
Fourth quarter	710	476	46	–	–	46
	$ 2,812	$ 1,950	$ 165	$ 28	$ –	$ 193

	Basic earnings per share of common stock				Diluted earnings per share of common stock			
	Continuing operations	Discontinued operations	Cumulative effect of change in accounting principles	Net income	Continuing operations	Discontinued operations	Cumulative effect of change in accounting principles	Net income
2002 (a)								
First quarter	**$ 0.26**	**$ –**	**$ (0.45)**	**$ (0.19)**	**$ 0.26**	**$ –**	**$ (0.45)**	**$ (0.19)**
Second quarter	**0.38**	**–**	**–**	**0.38**	**0.38**	**–**	**–**	**0.38**
Third quarter	**0.37**	**–**	**–**	**0.37**	**0.37**	**–**	**–**	**0.37**
Fourth quarter	**0.37**	**–**	**–**	**0.37**	**0.37**	**–**	**–**	**0.37**
	$ 1.38	**$ –**	**$ (0.45)**	**$ 0.93**	**$ 1.37**	**$ –**	**$ (0.45)**	**$ 0.92**
2001 (a)								
First quarter	$ 0.18	$ 0.02	$ –	$ 0.20	$ 0.18	$ 0.02	$ –	$ 0.20
Second quarter	0.28	0.15	–	0.43	0.28	0.15	–	0.43
Third quarter	0.28	–	–	0.28	0.28	–	–	0.28
Fourth quarter	0.29	–	–	0.29	0.29	–	–	0.29
	$ 1.04	$ 0.17	$ –	$ 1.21	$ 1.03	$ 0.17	$ –	$ 1.20

(a) The sum of amounts shown for individual quarters may not equal the total for the year because of changes in the weighted-average number of shares outstanding throughout the year.

The preceding notes are an integral part of the foregoing financial statements.

Selected Financial Data

For the years ended December 31 (In millions, except per-share data)	2002	2001	2000	1999	1998
Statement of Income (Loss)					
Sales					
Consumer and Foodservice/Food Packaging	**$ 2,062**	$ 1,997	$ 2,201	$ 2,132	$ 2,048
Protective and Flexible Packaging	**818**	815	851	896	835
Other	**–**	–	–	–	6
	2,880	2,812	3,052	3,028	2,889
Income (loss) from continuing operations before interest expense, income taxes, and minority interest	**463**	391	341	(13)	283
Interest expense, net of interest capitalized	**96**	107	134	146	133
Income tax expense (benefit)	**146**	118	91	(47)	67
Minority interest	**1**	1	3	–	1
Income (loss) from continuing operations	**220**	165	113	(112)	82
Income (loss) from discontinued operations, net of income tax	**–**	28	134	(193)	57
Extraordinary loss, net of income tax	**–**	–	–	(7)	–
Cumulative effect of change in accounting principles, net of income tax	**(72)**	–	–	(32)	–
Net income (loss)	**$ 148**	$ 193	$ 247	$ (344)	$ 139
Average number of shares of common stock outstanding					
Basic	**158.618**	158.833	161.722	167.405	168.506
Diluted	**160.613**	159.527	161.779	167.663	168.835
Earnings (loss) per share					
Basic					
Continuing operations	**$ 1.38**	$ 1.04	$ 0.70	$ (0.67)	$ 0.49
Discontinued operations	**–**	0.17	0.83	(1.15)	0.34
Extraordinary loss	**–**	–	–	(0.04)	–
Cumulative effect of change in accounting principles	**(0.45)**	–	–	(0.19)	–
	$ 0.93	$ 1.21	$ 1.53	$ (2.05)	$ 0.83
Diluted					
Continuing operations	**$ 1.37**	$ 1.03	$ 0.70	$ (0.67)	$ 0.49
Discontinued operations	**–**	0.17	0.83	(1.15)	0.34
Extraordinary loss	**–**	–	–	(0.04)	–
Cumulative effect of change in accounting principles	**(0.45)**	–	–	(0.19)	–
	$ 0.92	$ 1.20	$ 1.53	$ (2.05)	$ 0.83
Statement of Financial Position					
Net assets of discontinued operations	**$ –**	$ –	$ 72	$ 195	$ 366
Total assets	**3,412**	4,060	4,341	4,588	4,798
Short-term debt including current maturities of long-term debt	**13**	7	13	325	595
Long-term debt	**1,224**	1,211	1,560	1,741	1,312
Debt allocated to discontinued operations	**–**	–	–	–	548
Minority interest	**21**	8	22	20	14
Shareholders' equity	**897**	1,689	1,539	1,350	1,776
Statement of Cash Flows					
Cash provided (used) by operating activities	**$ 384**	$ 371	$ 290	$ (31)	$ 577
Cash provided (used) by investing activities	**(244)**	(1)	302	(994)	(514)
Cash provided (used) by financing activities	**(57)**	(354)	(578)	1,030	(67)
Expenditures for property, plant, and equipment	**(126)**	(145)	(135)	(173)	(194)

Corporate Information

DIRECTORS

Larry D. Brady
Chairman and Chief Executive Officer
UNOVA, Inc.

Robert J. Darnall
Retired Chairman and Chief Executive Officer
Inland Steel Industries

Mary R. (Nina) Henderson
Former Corporate Vice President
Bestfoods

Roger B. Porter
IBM Professor of Business & Government
Harvard University

Paul T. Stecko
Chairman and Chief Executive Officer
Packaging Corporation of America

Norman H. Wesley
Chairman and Chief Executive Officer
Fortune Brands, Inc.

Richard L. Wambold
Chairman and Chief Executive Officer
Pactiv Corporation

OFFICERS

Richard L. Wambold
Chairman and Chief Executive Officer

Andrew A. Campbell
Senior Vice President and Chief Financial Officer

James V. Faulkner, Jr.
Vice President and General Counsel and Secretary

Lisa K. Foss
Vice President, Communications

Monique C. Hines
Vice President and Chief Information Officer

Peter J. Lazaredes
Senior Vice President and General Manager
Foodservice/Food Packaging

James D. Morris
Senior Vice President and General Manager
Protective and Flexible Packaging

John N. Schwab
Senior Vice President and General Manager
Hefty® Consumer Products

Henry M. Wells, III
Vice President and Chief Human Resources Officer

Shareholder Information

Corporate Headquarters
Pactiv Corporation
1900 West Field Court
Lake Forest, IL 60045

Annual Meeting
Pactiv Corporation's annual meeting will be held at 10:30 a.m. Central time on May 16, 2003, at the Hilton Northbrook, Northbrook, Illinois

Transfer Agent and Registrar
National City Bank
Corporate Trust Operations
P.O. Box 92301
Cleveland, OH 44193-0900
Telephone: 866-770-1289
Hearing Impaired: 800-622-5571; 216-257-7353
Fax: 216-257-8508
E-mail: shareholder.inquiries@nationalcity.com
Notices regarding changes of address and inquiries concerning lost or stolen certificates and transfers of stock should be directed to the transfer agent.

Common Stock
Listed in the United States on the New York Stock Exchange, and traded under the symbol PTV.

SEC Filings and Other Information
Copies of the annual report, filings with the Securities and Exchange Commission, and press releases may be obtained by writing to:
Pactiv Corporation
Investor Relations Department
1900 West Field Court
Lake Forest, IL 60045
Or calling toll-free: 866-456-5439
Or via e-mail: investorrelations@pactiv.com

Investor Relations
Christine J. Hanneman
Vice President, Investor Relations
847-482-2429

Media Relations
Lisa K. Foss
Vice President, Communications
847-482-2704

Website
www.pactiv.com

Note: Trademarks owned by the Company or its subsidiaries are indicated by the use of italics, ®, or ™ throughout this report.

(seated)

Richard L. Wambold
Chairman and Chief Executive Officer

(standing from left to right)

John N. Schwab
Senior Vice President and General Manager
Hefty® Consumer Products

Andrew A. Campbell
Senior Vice President and Chief Financial Officer

James D. Morris
Senior Vice President and General Manager
Protective and Flexible Packaging

Peter J. Lazaredes
Senior Vice President and General Manager
Foodservice/Food Packaging